Notes

Right of Indemnitors of Co-tortfeasors to Contribution from Each Other

It has been stated as a general rule that one of two tortfeasors who satisfies a joint judgment recovered against them both, cannot obtain contribution from his co-tortfeasor.[1] The reasons usually advanced for this rule are that the enforcement of contribution would encourage the commission of torts, and that the courts will not aid wrongdoers. Not only has doubt been cast on the validity of these reasons, but other considerations of public policy make contribution desirable.[2] Accordingly, the rule has been riddled with exceptions and limitations by many courts and legislatures,[3] and there is a commendable tendency to prevent its extension whenever possible.[4] The Ohio court has recently rejected an opportunity to follow this tendency. A joint judgment of $7500 and costs was obtained against *A* and *B*, two motor companies, as concurrently negligent joint tortfeasors. Both *A* and *B* carried indemnity insurance, *A* with the plaintiff casualty company, and *B* with the defendant indemnity company. A statute provided that the liability of a tortfeasor's indemnitor should become absolute on the occurrence of the tort, and that a person obtaining a final judgment against the tortfeasor, which remained unsatisfied for thirty days after rendition, could then sue the indemnitor directly for the insurance money.[5] The defendant indemnity company refused to pay the judgment creditor more than $1000, and twenty-two days after the judgment was affirmed—but over a year after the rendition of the original judgment—the plaintiff casualty company paid the balance in order to prevent levy of execution on *A's* property. Thereafter, the casualty company instituted suit against the indemnity company for contribution. The court dismissed the suit, holding that contribution was unavailable because the parties were not co-sureties.[6]

The basis for recovery naturally suggested by this situation was subrogation of the plaintiff, *A's* indemnitor, to *A's* rights against others.[7] But if *A* had satisfied the judgment, the Ohio courts would have denied it contribution from *B*,[8] and consequently *B's* indemnitor.[9] The plaintiff could hardly have obtained a greater right

1. Union Stock Yards Company of Omaha v. Chicago, Burlington and Quincy Railroad Company, 196 U. S. 217 (1905).

2. An excellent criticism of the rule and the reasons supposedly underlying it may be found in Leflar, *Contribution and Indemnity Between Tortfeasors* (1932) 81 U. of Pa. L. Rev. 130.

3. See Union Stock Yards Company of Omaha v. Chicago, Burlington and Quincy Railroad Company, 196 U. S. 217, 224 (1905); Leflar, *supra* note 2, at 139-142, 144-145.

4. See Leflar, *supra* note 2, at 141-142.

5. Ohio Gen. Code (Page 1926) § 9510-3, 9510-4. Many other states have statutes which in some way make the indemnitor liable to the injured party. See Vance, Insurance (2d ed. 1930) § 178; Note (1933) 85 A. L. R. 20.

6. United States Casualty Company v. Indemnity Ins. Co. of North America, 129 Ohio St. 391, 195 N. E. 850 (1935) (Williams, J., dissented).

7. An indemnitor ordinarily may be subrogated to his indemnitee's rights against others. See Vance, op. cit. *supra* note 5, § 175.

8. Royal Indemnity Co. v. Becker, 122 Ohio St. 582, 173 N. E. 194 (1930).

9. Even where tortfeasor *A* has a right to contribution from his co-tortfeasor, *B*, he may not have any such right against *B's* indemnitor. In the absence of statute, *B's* indemnitor is usually liable only to *B*. Vance, op. cit. *supra* note 5, § 178. Statutes making the indemnitor directly liable to the tortfeasee are quite numerous. *Ibid.* But, despite

when placed in *A's* shoes through subrogation.[10] Another possibility of recovery was through subrogation to the judgment creditor's rights. A joint tortfeasor's surety, when compelled under his contract to pay the loss to the injured party, has sometimes been partially subrogated to the injured party's judgment rights against the other tortfeasor, thus obtaining contribution unavailable to his principal.[11] Accordingly it has been suggested that an indemnitor who fulfills his statutory duty by paying the injured party directly should be similarly treated.[12] No compelling reason appears why this should not be done.[13] But judicial precedent seems lacking, and the Ohio court has explicitly denied such relief, even where the indemnitor was also a surety on its indemnitee's appeal bond.[14]

The plaintiff sought to avoid these difficulties by relying on the entirely independent[15] doctrine of contribution, operating directly between the indemnitors. The court virtually decided the case by its supposition that contribution was avail-

such a statute, the New York court has refused to allow *A's* indemnitor to recover from *B's* indemnitor, seemingly because *A* had no such right. Metropolitan Casualty Insurance Company of New York v. Union Indemnity Company of Louisiana, 141 Misc. 792, 253 N. Y. Supp. 324 (Sup. Ct. 1929), aff'd without op., 255 N. Y. 591, 175 N. E. 326 (1931), noted in (1931) 16 CORN. L. Q. 400. But see Western Casualty & Surety Co. v. Milwaukee General Const. Co., 213 Wis. 302, 251 N. W. 491 (1933) *semble;* Langmaid, *Subrogation in Suretyship and Insurance* (1934) 47 HARV. L. REV. 976, 1005.

10. This conclusion has been criticised because the reasons for the rule as between tortfeasors have no application to their indemnitors. See Langmaid, *supra* note 9, at 1007; (1934) 32 MICH. L. REV. 1011. But the cases seem unanimously opposed to this argument. Adams v. White Bus Line, 184 Cal. 710, 195 Pac. 389 (1921); Royal Indemnity Co. v. Becker, 122 Ohio St. 582, 173 N. E. 194, 75 A. L. R. 1481 (1930); Cain v. Quannah Light & Ice Co., 131 Okla. 25, 267 Pac. 641 (1928) and see note 9, *supra.*

11. Kolb v. National Surety Co., 176 N. Y. 233, 68 N. E. 247 (1903); City of White Plains v. Ellis, 113 Misc. 5, 184 N. Y. Supp. 444 (1920), aff'd 200 App. Div. 869, 192 N. Y. Supp. 920 (1922), noted in (1921) 5 MINN. L. REV. 370; Rosenthal v. New York Rys. Co., 109 Misc. 210, 179 N. Y. Supp. 593 (Sup. Ct. 1919); see Smith v. Fall River Joint Union High School Dist., 1 Cal. (2d) 331, 334, 34 Pac. (2d) 994, 996 (1934). New York now allows contribution between tortfeasors by statute. N. Y. CIV. PRAC. ACT (1928) § 211a. But the same theory of subrogation to the judgment creditor's rights is still followed. Martin v. Miller, 242 App. Div. 38, 272 N. Y. Supp. 914 (1934).

12. See United States Casualty Company v. Indemnity Ins. Co. of North America, 129 Ohio St. 391, 399, 195 N. E. 850, 854 (1935) (Williams, J., dissenting: "It is the statutory obligation which is involved here and if the one insurance company which paid more than the other to the judgment creditor stood in the shoes of any one, it was in those of the judgment creditor"); Campbell, *Non-Consensual Suretyship* (1935) 45 YALE L. J. 69.

13. See Campbell, *supra* note 12, at 94.

14. Royal Indemnity Co. v. Becker, 122 Ohio St. 582, 173 N. E. 194 (1930) (The court did not discuss the effect of the statute). In accord: Smith v. Fall River Joint Union High School Dist., 1 Cal. (2d) 331, 34 Pac. (2d) 994 (1934); cf. Quatray v. Wicker, 178 La. 289, 151 So. 208 (1933). Both California and Louisiana also have statutes allowing the injured party to proceed directly against the indemnitor. GEN. LAWS OF CAL. (1931) Act. 3738, § 1; LA. GEN. STAT. (2 Dart 1932) § 4248.

15. Contribution does not depend on subrogation. Camp v. Bostwick, 20 Ohio St. 337 (1870); Central Banking & Security Company v. United States Fidelity & Guaranty Company, 73 W. Va. 197, 80 S. E. 121 (1913) (Suggests that courts sitting at law enforce contribution but not subrogation, and hence the concepts are not interdependent); see (1921) 5 MINN. L. REV. 370.

able only if the parties were co-sureties,[16] meaning thereby that both parties must be under a duty to satisfy the debt of the same person. But analysis shows that contribution is not so limited,[17] but is a flexible doctrine of equity,[18] applicable in many varying situations where it is desirable to prevent unjust enrichment.[19] Its essential elements appear to be: (1) a class of parties, each of whom is equally subject to a common burden, consisting of a risk, either of loss, or of failure to gain a benefit; (2) a payment, or its equivalent, by one of the parties, relieving the others of this risk; (3) a probability at the time of payment that the burden will fall on the class or a member thereof, sufficient to make the payment non-officious;[20] (4) the absence of a contract or rule of public policy prohibiting contribution.

If the plaintiff's payment in the principal case occurred more than thirty days

16. See United States Casualty Company v. Indemnity Ins. Co. of North America, 129 Ohio St. 391, 394, 195 N. E. 850, 852 (1935). Strictly speaking, the indemnitors were of course not co-sureties. Courts have sometimes explained their enforcement of contribution by calling the parties co-sureties. Vian v. Hilberg, 111 Neb. 232, 196 N. W. 153 (1923). This seems perfectly proper if the term is used only to describe the legal conclusion to which the court has come. But use of the term in a strict sense as an exclusive test to determine whether contribution is available is unjustifiable. The true test should be found in the factual situation, and not in legal nomenclature.

17. The right to contribution is not limited to parties liable for the debt of another, but is enforceable between joint principal debtors. Quintin v. Magnant, 285 Mass. 450, 189 N. E. 209 (1934). And it may arise from a statutory liability. Wolters v. Henningsan, 114 Cal. 433, 46 Pac. 277 (1896); Aspinwall v. Sacchi, 57 N. Y. 331 (1874); Manthey v. Schueler, 126 Minn. 87, 147 N. W. 824 (1914); Umsted v. Buskirk, 17 Ohio St. 113 (1866). Nor is it necessary to contribution that the parties be under a legal duty at all. For example, contribution is enforced between co-tenants where one has made necessary repairs. Fowler v. Fowler, 50 Conn. 256 (1882); between beneficiaries of a life insurance policy who accept its benefits after one has paid the necessary premiums. Stockwell v. Mutual Life Ins. Co., 140 Cal. 198, 73 Pac. 833 (1903); and between persons deriving benefit from litigation, the costs of which have been borne by one of their number. Maney v. Casserly, 134 Mich. 252, 96 N. W. 478 (1903).

18. Contribution originated in equity and was subsequently adopted by the law courts. Wayland v. Tucker, 4 Gratt. 267 (Va. 1848).

19. See Leflar, *supra* note 2, at 136; (1925) 35 YALE L. J. 92.

20. Payment has been deemed non-officious when made under the following circumstances: (a) Involuntarily, as where a party's securities, wrongfully pledged along with those of other parties by a common agent, have been sold by the pledgee: Asylum of St. Vincent De Paul v. McGuire, 239 N. Y. 375, 146 N. E. 632 (1925). (b) Under a legal duty, before suit: Shattuck v. Ellis, 49 Idaho 330, 288 Pac. 162 (1930); Western Casualty & Surety Co. v. Milwaukee General Const. Co., 213 Wis. 302, 251 N. W. 491 (1933). (c) Under a legal duty subject to a condition precedent, as where payment of an obligation is made before the due date: Golsen v. Brand, 75 Ill. 148 (1874); Hotham v. Berry, 82 Kan. 412, 108 Pac. 801 (1910); Craig v. Craig, 5 Rawle 91 (Pa. 1835); see Guckenheimer & Bros. Co. v. Kann, 243 Pa. 75, 80, 89 Atl. 807, 808 (1914). But it has been held that the party seeking contribution must show that the obligation would have accrued and not been satisfied otherwise: Loftus v. Tucker, 272 Ill. App. 245 (1933); see Hotham v. Berry, 82 Kan. 412, 414, 108 Pac. 801, 802 (1910). In such cases the right to contribution arises on the due date. Truss v. Miller, 116 Ala. 494, 22 So. 863 (1897). (d) Voluntarily, and under no legal pressure, where the class receives a positive benefit: Hill v. Crocker, 87 Me. 208, 32 Atl. 878 (1895); Stockwell v. Mutual Life Ins. Co., 140 Cal. 198, 73 Pac. 833 (1903); Maney v. Casserly, 134 Mich. 252, 96 N. W. 478 (1903). The common factor implicit in all these situations seems to be the strong probability that one or more of the class would sustain the burden, if the payment were not made.

after the "final judgment" indicated by the statute, these requirements would clearly have been met. (1) For, under the statute, the judgment creditor had a right to immediate payment from the indemnitor upon the elapse of thirty days from "final judgment" without payment by the judgment debtor. The indemnitors were thus subjected to an equal risk of having to pay the same judgment to the same person. (2) Payment by the plaintiff relieved the defendant of this risk. (3) The payment was non-officious because the plaintiff was under a legal duty to pay which he could not have resisted.[20] Nor is this altered by the fact that *A* might have satisfied the judgment, thus relieving both indemnitors of the risk of having to pay the judgment creditor. A surety who pays his principal's obligation on maturity without awaiting suit, may be allowed contribution from his co-surety without first showing that the principal would not have paid.[21] (4) No contract[22] or rule of public policy required the denial of contribution. The reasoning invoked to deny contribution between co-tortfeasors can have no application to their indemnitors, whose interests are opposed to the commission of torts, and who come into court with clean hands.[23] Nor can it be argued that to allow contribution between the indemnitors is to lighten the tortfeasors' load, and thus to evade the rule against contribution between co-tortfeasors. For the tortfeasors are held harmless in any event under their contracts with the indemnitors.[24]

If, then, the words "final judgment" in the Ohio statute mean the judgment of the trial court,[25] the plaintiff in the instant case should have been allowed to recover. For plaintiff did not make payment to the judgment creditor until over a year after the trial court judgment (but twenty-two days after judgment on appeal), and therefore, under the above construction of the statute, well beyond the elapse of the thirty-day statutory period without the judgment debtor having made payment. Thus, plaintiff might have been held to have paid the judgment creditor while under a legal duty to make immediate payment, and consequently to be entitled to contribution.[26]

But if the term "final judgment" refers to the final disposition of the case on appeal, the plaintiff's payment was made within the thirty day period, and the

21. Odlin v. Greenleaf, 3 N. H. 270 (1825); see Buckner v. Stewart, 34 Ala. 529, 535 (1859). This question usually arises where the surety has been compelled to pay the creditor, and is discussed from the standpoint of whether the surety has exhausted his remedies, rather than as a question of officiousness. See Note (1924) 29 A. L. R. 273.

22. The court argued that contribution would extend the defendant's liability beyond the scope its bond was intended to cover. But contracting under the statute, the defendant was bound to pay, either to the judgment creditor or to its indemnitee, the full loss occasioned by an accident for which its indemnitee was responsible. Compelling payment of half this loss would hardly be an extension of this contract.

23. See (1934) 32 MICH. L. REV. 1011; (1931) 79 U. OF PA. L. REV. 507.

24. It is sometimes argued that allowing sureties contribution would in effect enable their principals to obtain contribution. But a distinction can be drawn between the case of a surety, who has recourse against his principal, and that of the indemnitor, who has no recourse against his indemnitee. See Langmaid, *supra* note 9, at 1007; (1931) 79 U. OF PA. L. REV. 507, 509.

25. The original judgment was certainly final in the sense that it was appealable.

26. The court suggested that the statute was intended for the benefit of judgment creditors, and no intent to give insurance companies a right to contribution could be inferred without express provision therefor. But it is only necessary that the statute create a right-duty relationship between the insurance companies and the judgment creditor. This established, equity provides the right to contribution without the aid of statute. In Umsted v. Buskirk, 17 Ohio St. 113 (1866), the court overruled a contention similar to that made by the court here.

question of officiousness becomes more difficult. Within that period, the plaintiff was under a duty to the judgment creditor, subject to the condition that thirty days from final judgment must first elapse without satisfaction of the judgment. Payment in such a situation apparently creates a right to contribution only if it appears certain that the common burden would not be borne by someone outside the class.[20] Here *A* or *B* might have satisfied the judgment, thus relieving both indemnitors of any risk of having to pay the judgment creditor. The concept of common burden in suits for contribution, however, seems broad enough to meet this difficulty. The entry of judgment against *A* and *B* subjected each indemnitor to an equal risk of having to bear the loss, either through payment to the judgment creditor by virtue of the statute, or to its indemnitee under its contract. This constituted a common burden, although the indemnitors originally undertook different risks,[27] being liable under independent contracts to different persons.[28] For contribution does not depend on original relationship,[29] and the judgment placed them in exactly equal positions. Furthermore, this common burden to which the indemnitors were subject would justify contribution between them, even if the equality of risk did not continue until the very moment of payment by one of the indemnitors; that is, if *A* satisfied the judgment, and thus relieved *B's* indemnitor of the risk before *A's* indemnitor paid *A*. For, as a general rule, where parties have been subject to a common burden, contribution is compelled even though at the time of payment, one of them has already been discharged, by a release or the running of the statute of limitations.[30] Accordingly, under the foregoing concept of a common burden, the plaintiff's payment was clearly non-officious. For the requirement of non-officious payment is intended to protect the class from contribution only where the class might have escaped the common burden had payment not been made,[20] and here the entry of judgment made it certain that one of the two indemnitors would have to bear the loss eventually even if *A* or *B* satisfied the judgment. Finally, the statute could not have been intended to prevent contribution, for obviously its only purpose was to facilitate the collection of judgments. Refusing the indemnitor contribution on the sole ground that payment was made within the thirty day period would encourage delay of payment until after the period, through any available means, thus defeating the purpose of the statute. If considering payment non-officious under these conditions involves any extension of previous conceptions, it is by no means unparalleled.[31]

Aside from strictly legal considerations, there are other reasons why contribution

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27. In National Surety Co. v. Massachusetts Bonding & Ins. Co., 19 Fed. (2d) 448 (C. C. A. 2d 1927), cert. denied, 275 U. S. 548 (1927), it was stated that contribution will not be enforced between insurers unless the risk insured is identical. But the important point is that because of the judgment, the indemnitors were subjected to exactly the same risk, and what they originally undertook should then have become of no significance. Cf. Agren v. Staker, 46 Idaho 36, 267 Pac. 460 (1928); Langmaid, *supra* note 9, at 996; (1927) 76 U. of Pa. L. Rev. 75. But cf. Southern Surety Co. v. Nichols, 239 Mich. 158, 214 N. W. 137 (1927).

28. Contribution is enforced between co-sureties although they become bound by separate instruments without knowledge of each other's undertaking. Robinson v. Boyd, 60 Ohio St. 57, 53 N. E. 494 (1899).

29. Asylum of St. Vincent De Paul v. McGuire, 239 N. Y. 375, 146 N. E. 632 (1925).

30. Kelly v. Sproul, 153 Mich. 691, 117 N. W. 327 (1908); Young v. Burnett, 81 N. H. 163, 127 Atl. 435 (1923); Johnson v. Harvey, 84 N. Y. 363 (1881); Camp v. Bostwick, 20 Ohio St. 337 (1870).

31. Cf. Manthey v. Schueler, 126 Minn. 87, 147 N. W. 824 (1914); Howie v. Gengloff, 165 Minn. 346, 206 N. W. 441 (1925); Pechtl v. Schmid, 172 Minn. 362, 215 N. W. 512 (1927).

would have been desirable.[32] Ordinary standards of justice are disregarded if the loss is allowed to fall by accident or according to the whim of the judgment creditor. More important, the denial of contribution between indemnitors offers a powerful inducement to collusion[33] between one of them and the judgment creditor. If the latter makes use of this opportunity to extort from the insurance companies more than the amount of his judgment, the burden ultimately falls on the insuring public. Again, while the burden of an insurance company may occasionally be lightened by receiving contribution where its indemnitee happens to be joined as a co-tort-feasor with another insured party, this remote possibility would hardly tend to lessen the care used in the choice and supervision of risks, particularly since the company may well have to make contribution to others for accidents in which its indemnitee becomes involved. Thus, while the extension of the doctrine of contribution to the situation here involved would apparently have been a slightly new departure,[34] there were sound reasons and ample legal justification for such action.

Amortization of Premiums and Accumulation of Discounts in the Administration of Trust Investments

When trust funds are invested in bonds, the income to go to a beneficiary for life, with remainders over, the problem arises of securing to the life tenant an adequate income, and at the same time, of preserving the corpus intact for the remainderman. A bond bought by the trustee at par involves no difficulties, since the entire interest is income payable to the life tenant. But when an investment is made in a bond purchased at a price greater than its face value, a larger sum is paid than will be returned when the bond is redeemed at par. To prevent the loss to corpus of this amount paid as premium, it is the usual practice of trustees to make proportionate deductions from each interest payment and apply them to a sinking fund which will be equal to the premium paid when the bonds are matured, thus leaving the principal of the estate unimpaired. Although the intention of the testator governs in all cases,[1] most courts hold that this practice is proper,[2] while in the minority of jurisdictions the loss of premium is held to devolve on the corpus, and hence is borne by the remainderman.[3]

32. Most of these other reasons suggested in the text are advanced in Campbell, *supra* note 12, at 94. And see Leflar, *supra* note 2, at 137.

33. Cf. Pennsylvania Co. v. West Penn. Rys. Co., 110 Ohio St. 516, 144 N. E. 51 (1924).

34. The only case found involving the same facts is Metropolitan Casualty Insurance Company of New York v. Union Indemnity Company of Louisiana, 141 Misc. 792, 253 N.Y. Supp. 324 (Sup. Ct. 1929), aff'd without opinion, 255 N. Y. 591, 175 N. E. 326 (1931) noted in (1931) 16 Corn. L. Q. 400. The plaintiff was there denied recovery, but the question of contribution directly between the indemnitors was apparently not considered.

1. Shaw v. Cordis, 143 Mass. 443 (1887); Re Hoyt, 160 N. Y. 607, 55 N. E. 282 (1889).

2. Curtis v. Osborn, 79 Conn. 555, 65 A. 968 (1907); New England Trust Co. v. Eaton, 140 Mass. 532, 4 N. E. 69 (1886), (Holmes, J., dissenting), criticized in (1886) 34 Alb. L. J. 144; In re Gartenlaub's Estate, 185 Cal. 648, 198 P. 209 (1921); Ballantine v. Young, 74 N. J. Eq. 572, 70 A. 668 (1908); In re Stevens, 187 N. Y. 471, 80 N. E. 358 (1907); In re Well's Estate, 156 Wis. 294, 144 N. W. 174 (1914).

3. American Security & Trust Co. v. Payne, 33 App. D. C. 178 (1909); Hite v. Hite, 93 Ky. 257, 20 S. W. 778 (1892); In re Penn-Gaskell's Estate, 208 Pa. 346, 57 A. 715 (1904). This was formerly the general rule even in those states where amortization is now compelled. Hemenway v. Hemenway, 134 Mass. 446 (1883); Matter of Pollock, 3 Redf. 100 (N. Y. Surr. Ct. 1877); Bergen v. Valentine, 63 How. Pr. 221 (N. Y. Sup. Ct. 1882); In re New York Life Ins. Co., 24 Misc. 71, 53 N. Y. S. 382 (Surr. Ct. 1898).

In the converse of the situation, where a bond is purchased at a discount and is later repaid at par, the few courts to which the question has been presented have been unanimous in refusing to compel trustees to accumulate the discount as income for the life tenant.[4] Both these problems arose in a recent Massachusetts case.[5] Trustees purchased bonds at a premium as an investment for part of a trust fund, and amortized the premium. Other bonds, bought at a discount, matured and were paid at par.[6] The difference between the lower price at which the latter bonds were purchased, and the amount realized at maturity, was credited to principal as a capital gain. In a bill for an accounting brought by the life tenant, it was claimed that, if there was to be amortization of premiums for the benefit of the remainderman, there should also be accumulated and credited to income the discount resulting from the purchase of bonds below par. The court held that amortization was proper, but rejected the claim of the life tenant on the ground that gains in the value of investments belong to capital, and are to be credited to the principal of the trust fund rather than to income.

In those jurisdictions where amortization is compelled, logical consistency would seem to demand accumulation, for the proposition which supports the one governs the other.[7] The theory upon which amortization is based is that a bond sells at a premium because it bears a rate of interest greater than the current market rate for similar securities.[8] Since such a bond will be redeemed only at par, each interest payment represents not the actual earning of the investment, but more, the excess being a return of a proportional part of the principal paid as premium.[9] Therefore deductions are made from each coupon payment, aggregating, at maturity, the amount of the premium. By this method of accounting, the life tenant has received as income no more than the investment has actually earned, and the full capital which was used to purchase the bond is restored to the corpus. In like manner proceeds the theory support-

4. In re Estate of Gartenlaub, 198 Cal. 204, 244 P. 348, 48 A. L. R. 677 (1926), noted in (1926) 15 CAL. L. REV. 66; In re Houston's Will, 19 Del. Ch. 207, 165 A. 132 (1933), noted in (1933) 47 HARV. L. REV. 143; Wood v. Davis, 168 Ga. 504, 148 S. E. 330 (1929); Townsend v. United States Trust Co., 3 Redf. 220 (N. Y. Surr. Ct. 1877). This latter case, however, was decided at a time when amortization of premiums was not yet recognized in New York. It was approved by way of dictum in Re Accounting of Gerry, 103 N. Y. 445, 9 N. E. 235 (1886), which is often cited as an authority opposed to accumulation of discounts. But it does not appear that the bonds in that case were bought below par. The question may still be considered an open one in New York.

5. Old Colony Trust Co. v. Comstock, 195 N. E. 389 (Mass. 1935).

6. Trustees purchased bonds having a par value of $13,000 for $12,973.13. Thus at maturity there was a realization of $26.87 more than the cost.

7. See Holmes, J. in Hemenway v. Hemenway, 134 Mass. 446, 450 (1883), and his dissent in New England Trust Co. v. Eaton, 140 Mass. 532, 544, 547, 4 N. E. 69, 77, 80 (1886); PERRY, TRUSTS (7th ed. 1929) § 548b.

8. This is graphically illustrated by the two bond issues recently offered by the Southern California Edison Company Ltd. In July, 1935, the Company offered a series of 3¾s, due 1960, at a price of 98½%. Two months later, a series of 4s, also due 1960, was offered at a price of 102%. The same security is behind both bond issues, and their respective yields to maturity are practically equal. See (July 6, 1935) 141 Commercial & Financial Chronicle, XII, and (Sept. 21, 1935) id. at VI. Theoretically, all bonds which are perfectly safe should be selling at such a price as will produce a net yield equal to the prevailing interest rate at the time of purchase. See Vierling, *Amortization of Premiums and Accumulation of Discounts on Trust Investments* (1923) 8 ST. LOUIS L. REV. 1, 3; ANNO. (1926) 48 A. L. R. 689. But see note 13, *infra*.

9. See In re Gartenlaub's Estate, 185 Cal. 648, 652, 198 P. 209, 210 (1921); In re Stevens, 187 N. Y. 471, 476, 80 N. E. 358, 359 (1907).

ing accumulation of discounts. A bond sells at a discount because it bears a rate of interest lower than the current market rate for securities of the same grade.[8] But since it will be redeemed at par, there is a rise in the value of the bond toward that figure as maturity approaches. This appreciation was contracted for at the time of purchase,[10] and represents to the trust estate not capital gain, but income earned and retained in the investment.[11] Thus the interest payments are a part only of what the bond actually is earning; the balance of the income is only realized when it is sold or matured at par. Consequently this accretion logically should not be added to corpus, but should accrue to the life tenant as income.

But while the majority of courts have recognized the principle of amortization in order to preserve the corpus intact,[2] they have rejected the argument for accumulation of discounts on the ground that factors other than a bond's interest rate may determine the price at which it will sell below par.[12] But it would seem that this is equally true of bonds selling at a premium.[13] A further objection is that payment of the accumulated income as it accrues would involve the sale of some of the corpus in order to find funds with which to make annual payments to the life tenant, and if the bond should later default or be sold at a loss before maturity, an additional decrement is suffered by the corpus.[14] However, the claim is merely that the accumulation should be paid to the life tenant only upon sale or maturity.[15] To this it may be objected that, by the time of realization, the life tenant may have died, or may not

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10. In this respect, increases by way of accumulating discount are to be distinguished from ordinary increases, which are accidental and unanticipated. Since this tendency of a discount bond to "appreciate" is inherent and certain, it may be considered as paid for at the time of the investment, being figured in the price at which the security is bought. See Vierling, *Accumulation of Discounts* (1926) 41 J. ACCOUNTANCY, 267, 276; CHAMBERLAIN AND EDWARDS, THE PRINCIPLES OF BOND INVESTMENT (rev. ed. 1927) 25, 27.

11. For example, the rate of net yield on a $1,000 bond bearing 4% interest and having 10 years to run, bought at $900.10 is approximately 5.30%. After six months the value of the bond at the same net yield will be about $903.90. No capital has been added, and it is apparent that this $3.80 gain in the invested sum represents earnings. See CHAMBERLAIN AND EDWARDS, THE PRINCIPLES OF BOND INVESTMENT (rev. ed. 1927) 524; George K. Black, *Amortization—An Unsettled Question in Trust Accounting* (1932) 17 MASS. L. Q. 81, 83.

12. "Purely accidental circumstances may be . . . important factors." In re Houston's Will, 19 Del. Ch. 207, 213, 165 A. 132, 134 (1933), quoted with approval in the instant case, at 392. The courts rejecting the principle of amortization of premiums do so for the same reason. See In re Penn-Gaskell's Estate, 208 Pa. 346, 348, 57 A. 715, 716 (1904).

13. That the premium is paid solely in respect of interest, which is the assumption supporting amortization, is a fiction, is demonstrated by any survey of bond prices. For example, Chile Copper Company's debenture 5s, due 1947, have ranged in price from 79 to 100¾ since January 1, 1935; Bell Telephone of Pennsylvania's 5s, series B, due 1948, have ranged from 113¼ to 120½ during the same period; Detroit Edison 5s, series A, due 1949 have fluctuated between 105⅝ and 109¾ during the same period. See (Oct. 12, 1935) 141 Commercial & Financial Chronicle, 2403, 2404. See Holmes, J. in Hemenway v. Hemenway, 134 Mass. 446, 449 (1883), and his dissent in New England Trust Co. v. Eaton, 140 Mass. 532, 544, 4 N. E. 69, 77 (1886).

14. See In re Houston's Will, 19 Del. Ch. 207, 212, 213, 165 A. 132, 134 (1933). For the converse reason, that securities bought at a premium may increase in value, the Kentucky and Pennsylvania courts rejected the principle of amortization. See In re Penn-Gaskell's Estate, 208 Pa. 346, 348, 349, 57 A. 715, 716 (1904); Hite v. Hite, 93 Ky. 257, 269, 20 S. W. 778, 780 (1892).

15. Gradual payment of the discount before realization would be payment of income before it is received by the trustee. This the trustee is under no duty to do, nor has it ever

be the same life tenant who is claimed to have lost the income.[16] Thus, the life tenant's receipt of the discount depends upon the contingencies that the bond will be redeemed at par, and that he will be alive to receive it. In this respect, discounts and premiums are on different planes. While the premium is paid out from corpus at the time of purchase of the bond, the discount remains only an intangibility until the bond is sold or matured at par. Influenced by these chance elements in trust investments, the Uniform Principal and Income Act[17] proposes to do away with both, and to charge all loss or gain from sale or redemption of bonds to principal, on the ground that workable rules and simplicity of administration are nearest the settlor's probable intent.[18] This appears to be a practical solution to an intricate problem, obviating mathematical and legal hair-splitting, and precluding much of the litigation which might arise from more detailed accounting practices.[19] Nor would the Act expose the capital to the danger of being exhausted. For the trustee's fear of being surcharged for any undue shrinkage of the corpus, counterbalanced by the life tenant's insistence upon an adequate income, would oblige the trustee to hold an even equilibrium between the opposing interests, with the result that in the long run, differences on both sides of the ledger would even themselves out. This procedure has been followed by the minority of courts,[3] and two jurisdictions have recently adopted it by statute.[20] The application of the same rule to both life tenant and remainderman has the merit of impartiality, and where courts do not approve accumulation of discounts, it would seem that fairness to the life tenant, who is, after all, the testator's nearest object of bounty, would demand the discarding of amortization. The application of one principal for premium bonds and another for discount bonds is both inconsistent and inequitable. A balanced justice would seem to require either full acceptance of the amortization-accumulation rule or adoption of the simpler Uniform Principal and Income Act.[21]

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been urged that he should. See Edgerton, *Premiums and Discounts in Trust Accounts* (1918) 31 Harv. L. Rev. 447, 467; George K. Black, *Amortization—An unsettled Question in Trust Accounting* (1932) 17 Mass. L. Q. 81, 85. But courts have always proceeded on the assumption that this was the method contemplated. See Holmes, J. dissenting in New England Trust Co. v. Eaton, 140 Mass. 532, 544, 547, 4 N. E. 69, 77, 80 (1886); In re Houston's Will, 19 Del. Ch. 207, 212, 213, 165 A. 132, 134 (1933).

16. See the instant case, at 392.

17. Section 6 (1931) 41 Handbook of the National Conference of Commissioners, 332, noted in (1932) 32 Col. L. Rev. 118, 121.

18. See (1931) 41 Handbook of the National Conference of Commissioners, 326.

19. There are three methods of amortizing. (1) The premium is charged out of the income at once, without taking into account the interest on the amortization fund up to the time of maturity of the bond. (2) The level method, by which an equal amount is deducted from each income payment during the life of the bond, again without considering the interest on the amortization fund. (3) The mathematical method, which necessitates a new computation at each interest payment date, taking account of interest on funds previously amortized. Only the last method is technically accurate, but to insist on it would inflict unnecessary hardship on trustees in many cases, especially where the premium is small. Other problems arise where a bond having a call date is bought. If the premium is amortized to the call date and price, and the bond is not called, a new amortization schedule has to be fixed. But the life tenant has been treated unfairly in the meantime.

20. Or. L. 1931, c. 371, § 6; Rev. L. Hawaii (1935) c. 135, § 4714.

21. Cf. Restatement, Trusts § 239, comment f, § 240, comment h.

THE USE OF THE DECLARATORY JUDGMENT IN PATENT CASES

When a patent is infringed, the patentee may at his election maintain an action for damages[1] or for an injunction coupled with damages[2] against an infringing manufacturer or his dealers.[3] A patentee has the further privilege of publicly alleging the supposed infringement and of warning the customers of the manufacturer of his intention to bring suit against all who deal in the product in question.[4] On the other hand, until the enactment of the Federal Declaratory Judgments Act,[5] an alleged infringer could not maintain an action against the threatening patentee to determine the validity of these allegations of infringement, but was compelled to await the patentee's infringement suit for an adjudication of his legal rights.[6] Since public allegations of infringement intimidate dealers into not handling the product and thereby seriously injure the manufacturer's business,[7] the patentee was so situated that by abusing his privileges he could usually force a settlement from the former without risking a judicial determination of any unfounded claims.[8] For a patentee could merely refuse to bring an action and confine his activities to public threats and warnings. He might go further and bring suit, advertising that fact to the trade, and, after postponing trial for some time, might finally effect a dismissal without prejudice.[9] Since a patentee may sue any infringer at his election, he could bring action against a remote dealer in the hope of obtaining a default judgment that he could employ to give more force to his claims of infringement. If the manufacturer attempted to intervene in such a suit, or if the dealer contested, the patentee then might ask for a dismissal without prejudice,

1. REV. STAT. § 4919 (1875), 35 U. S. C. A. § 67 (1929).

2. 42 STAT. 392 (1922), 35 U. S. C. A. § 70 (1929).

3. See Foote v. Parsons Non-Skid Co., 196 F. 951, 953 (C. C. A. 6th, 1912); Elliot Co. v. Roto Co., 242 F. 941, 942 (C. C. A. 2d, 1917); I. T. S. Rubber Co. v. Essex Rubber Co., 270 F. 593, 608 (D. Mass., 1920). Under Equity Rule 37, the manufacturer might be allowed to intervene in the action against his dealer (Rules of Practice for courts of Equity as amended to 1932).

4. See Clip Bar Mfg. Co. v. Steel Protected Concrete Co., 209 F. 874, 875 (E. D. Pa., 1913) and cases there cited.

5. 48 STAT. 955, 28 U. S. C. A. § 400 (1934).

6. See Mowry v. Whitney, 81 U. S. 434, 441 (1871); Celluloid Mfg. Co. v. Goodyear Dental Vulcanite Co., Fed. Cas. No. 2,543 at 349, 350 (C. C. S. D. N. Y., 1876).

7. See Price Hollister Co. v. Worford, 18 F. (2d) 129, 130 (S. D. N. Y., 1926) (alleged infringer's trade had been decreased by 60% in less than one year because of the intimidation). See also Robb, *Suggestions for Patent Law Revision* (1925) 7 J. PATENT OFFICE SOCIETY 424, 427; SPENCER, UNITED STATES PATENT LAW SYSTEM (1931) 47, 48. Cf. TERRELL, PATENTS (English), (1934) 355, 356, 365.

8. See SPENCER, UNITED STATES PATENT LAW SYSTEM (1931) 47; WAITE, PATENT LAW (1920) 299, 300.

9. See United Motors Service Inc. v. Tropic Aire Inc., 57 F. (2d) 479 (C. C. A. 8th, 1932); Thomson-Houston Electric Co. v. Holland, 160 F. 768 (C. C. N. D. Ohio, 1907); Pennsylvania Globe Gaslight Co. v. Globe Gaslight Co., 121 F. 1015 (C. C. Mass., 1902). However, where the dismissal would affect a "substantial right" of the defendant, it cannot be obtained without prejudice. See Pullman's Palace Car Co. v. Central Transportation Co., 171 U. S. 138, 146 (1897); Dooley Improvements Inc. v. Motor Improvement Inc., 6 F. Supp. 161, 162 (D. Del., 1934). In patent cases, it has been held that the mere annoyance of another action is not sufficient to deprive defendant of a substantial right. See N. Y. Life Ins. Co. v. Driggs, 72 F. (2d) 833, 834 (C. C. A. 4th, 1934); Staude Mfg. Co. v. Labombarde, 229 F. 1004, 1006 (D. N. H., 1916); Young v. Samuels & Brother, Inc., 232 F. 784, 785 (D. R. I., 1916); cf. Lunati v. Marnoll Steel Products Co., 10 F. Supp. 282 (E. D. N. Y., 1935); A. C. Gilbert Co. v. United Electrical Mfg. Co., 33 F. (2d) 760 (E. D. Mich., 1929).

and thus prevent any judicial adjudication of his claims. Only when the patentee abused his privileges so flagrantly as to be guilty of unfair competition, was a measure of relief available to the alleged infringer. In that case, if the latter could demonstrate that the patentee was acting with malicious intent to destroy the infringer's property, or in bad faith, which is evidenced by failure to bring suit over an unreasonable period of time, an injunction might be obtained against the continuance of the allegations of infringement and the threats of suit.[10] But the efficacy of this relief is questionable, since the action for injunction is concerned only with unfair competition and cannot determine the issue of infringement.[11]

The enactment of the Federal Declaratory Judgment Act[5] gave rise to expectations that this abuse of a patentee's privileges could now be halted.[12] For the declaration seems to provide a means whereby an immedaite adjudication of issues raised by allegations of infringement may be obtained by the alleged infringer, and unfounded assertions quickly silenced.[13] One of the first attempts to realize these possibilities was made in the recent case of *Zenie Bros. v. Miskend.*[14] Here the defendant patentee had threatened the petitioner and his customers with actions for infringement, but had declined to bring suit. The alleged infringer thereupon petitioned for a declaration that the patents in question were void for want of invention and that consequently he had not infringed upon a valid patent. The latter's motion to dismiss the peittion, on the ground that the court had no jurisdiction of a petition of this character, was denied.[15]

10. Racine Paper Goods Co. v. Dittgen, 171 F. 631 (C. C. A. 7th, 1909) (threats for 7 years); Atlas Underwear Co. v. Cooper Underwear Co., 210 F. 347 (E. D. Wis., 1913); Andriance Platt & Co. v. National Harrow Co., 121 F. 827 (C. C. A. 2d, 1903) (threats continued for 6 years); Sun Maid Raisin Growers v. Avis, 25 F. (2d) 303 (N. D. Ill., 1928) (threats for 2 years). But cf. Kidd v. Horry, 28 F. 773 (C. C. E. D. Pa., 1886); Steward Davit and Equipment Corp. v. Welin Davit and Boat Co., 299 F. 610 (E. D. N. Y., 1924); Deyhydro v. Trelolite Co., 53 F. (2d) 273, 274 (N. D. Okl., 1931); Boston Diatite Co. v. Florence Mfg. Co., 114 Mass. 69 (1873).

11. See Emack v. Kane, 34 F. 46, 51 (C. C. N. D. Ill., 1888).

12. Comment (1934) 8 Univ. of Cinn. L. Rev. 523, 528. See also Rossman, *Declaratory Judgment* (1935) 17 J. Patent Office Society 1; cf. *Revision of American Patent Laws* (1934) 16 J. Patent Office Society 731, 741; O'Brien, *Restrictions upon the Usefulness of Declaratory Judgment in Patent Suits* (1935) 17 J. Patent Office Society 270, 274, 275. The English patent statute specifically allows a threatened infringer to have recourse to a declaration that such threats are unjustified. See The Patents and Designs Act, 7 Edw. VII, c. 29 § 36 (1) (1907), as amended by 22 & 23 Geo. V, c. 32, § 6 (1) (1932). See also Terrell, op. cit. *supra* note 7, at 356, 365.

13. See Borchard, Declaratory Judgments (1934) 25, 26, 583. The declaration may be thus utilized not only in a direct petition, but by way of counterclaim in the patentee's action for infringement. This procedure would prevent any dismissal without prejudice of the original action (see note 9 *supra*). See Harris, *Counterclaiming for Declaratory Relief* (1935) 17 J. Patent Office Society 244; also report of two recent cases in Note (1935) 17 J. Patent Office Society 674.

14. 10 F. Supp. 779 (S. D. N. Y., 1935). See cases reported by Rossman, op. cit. *supra* note 12, at 5-9, and also Lionel Corp. v. DeFilippis, 11 F. Supp. (E. D. N. Y. 1035) 712.

15. Compare the decision in the principal case (note 14, *supra*) with Automotive Equipment Inc. v. Trico Products Corp., 11 F. Supp. 292 (W. D. N. Y., 1935) where petition for declaration of non-infringement was dismissed as unnecessary because the patentee had previously brought action against certain customers of the petitioner for infringement and all issues raised by the petition could therefore be determined on petitioner's intervention in that suit.

The contention that the federal courts may not hear an alleged infringer's petition for declaratory judgment is based upon his previous inability to maintain an action against the patentee to determine the validity of charges of infringement.[9] It is argued, in the first place, that these allegations are mere assertions by the patentee of his rights, and do not constitute injuries to the alleged infringer which can be corrected or prevented by judicial action.[16] However, this argument overlooks the fact that an actual injury is not a prerequisite to obtaining judicial relief by declaration. The declaratory judgment recognizes the right of a person to remain free from unjustified claims that disturb the security of his legal interests, and accordingly offers a means whereby immunity to such claims may be judicially established.[17] It is further contended, however, that equitable relief has hitherto been denied to the alleged infringer on the ground that a patent is a government grant, and may therefore not be attacked by a private party,[18] and that this objection still prevails against a petition for a declaration of non-infringement. But the early concept of a patent as an inviolate government grant has been largely modified, and a patent is now recognized as a private monopoly exercised for private profit.[19] Under the patent laws a suit in equity could always be maintained by a private party to cancel an interfering patent,[20] and an unsuccessful applicant, by asking for a judicial adjudiction of his right to a patent, could obtain a determination of the validity of a prior patent.[21] Although no specific statutory provision has been made to allow a person to obtain a judicial decision on the validity of a patent which he is alleged to have infringed, the Declaratory Judgment Act[5] was passed for the express purpose of affording a remedy in cases not formerly susceptible of judicial relief under the then existing forms. The Act makes no exception of patent cases, and since it provides a remedy which is eminently suited to relieve the harsh position in which alleged patent infringers have been heretofore placed, a petition for a declaration of non-infringement of a patent should be entertained by the federal courts.[22]

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16. Judicial relief could be obtained only when the defendant's conduct constituted unfair competition. Cf. notes 10 and 11, *supra*.

17. See BORCHARD, op. cit. *supra* note 13, at 38, 91, 319, 335, 386-389, 419-421. In English practice, the possibility of a mere declaration of a no-right in the party against whom the declaratory judgment is sought was first appreciated after the adoption of the rule making unnecessary the issuance of consequent relief after declarations of rights. Compare part (1) of present Federal Act, 48 STAT. 955, 28 U. S. C. A. § 400 (1934). See Guaranty Trust Co. of N. Y. v. Hannay & Co. (1915) 2 K. B. 536, 565 (declaration of petitioner's immunity to claims based on forged bills of lading); Dyson v. Att'y-General (1911) 1 K. B. 410, (1912) 1 Ch. 158; Burghes v. Att'y-General (1911) 2 Ch. 139, (1912) 1 Ch. 173 (petitioner's immunity to a government demand).

18. Cf. Mowry v. Whitney, 81 U. S. 434, 441 (1871).

19. See Fox Film Corp. v. Doyal, 286 U. S. 123, 130 (1932), overruling Long v. Rockwood, 277 U. S. 142 (1928), which had denied the state's power to tax income derived from patents. Moreover, a patent is surely not more inviolate than a statute, and yet a declaration may be used to attack the latter's validity. Penn v. Glenn, 10 F. Supp. 483 (W. D. Ky., 1935) (decision overruled by statute as regards the use of the declaration to prevent collection of taxes), noted in (1935) 44 YALE L. J. 1451; see Borchard, op. cit. *supra* note 13, at 552, 553.

20. REV. STAT. § 4918 (1875), 35 U. S. C. A. § 66 (1929).

21. REV. STAT. § 4915 (1875), 35 U. S. C. A. § 63 (1929).

22. See Jaeger v. Jaeger, 44 REP. PAT. CASES 83 (1927); Killen v. MacMillan, 49 REP. PAT. CASES 258, 261 (1932); cf. Traction Corp. v. Bennett, 25 REP. PAT. CASES 819 (1908); North Eastern Marine Engineering Co. v. Leeds Forge Co. (1906) 1 Ch. 324, aff'd (1906) 2 Ch. 498; Felt Gas Compressing Co. v. Felt (1913) 14 D. L. R. 395. Of significant interest,

The further argument[23] that recognition of this procedure in patent cases would hamper the patentee in the enjoyment of his exclusive monopoly contrary to the intent of Congress, because he would be subjected to a multiplicity of vexatious actions brought all over the country by parties desirous of establishing non-infringement,[24] disregards the fact that the existence of a controversy is a requisite to declaratory relief.[25] Since no controversy can exist here until the patentee has made a demand upon the alleged infringer, or threatened suit against him or his customers, the number of actions that are brought depends solely upon the patentee.[26] Moreover, if he has threatened suit in good faith, and an infringement of a valid patent does exist, then he ought not to object to the infringer's action for declaratory relief, for he can there obtain an adjudication of the same issues which would be presented by his suit for patent infringement.

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because of its resemblance to the declaratory process, is a practice common in the Sixth Circuit. Here, after an adjudication of patent infringement in the suit by patentee, the court on application by the defendant will declare whether a new model or specification would also infringe upon said patent. See Kalamazoo Loose Leaf Binder Co. v. Proudfit Loose Leaf Co., 243 F. 895, 898 (C. C. A. 6th, 1917); Knabe Bros. Piano Co. v. American Piano Co., 232 F. 140, 141 (C. C. A. 6th, 1916); cf. Hollingshead Co. v. Bassick Mfg. Co., 50 F. (2d) 592, 593 (C. C. A. 6th, 1931); Cincinnati Car Co. v. N. Y. Rapid Transit Corp., 52 F. (2d) 44, 45 (C. C. A. 2d, 1931).

23. Another argument against allowing a petition for a declaration of non-infringement is that it merely anticipates the defense that would ordinarily be interposed to the patentee's action for infringement, and therefore should be dismissed as unnecessary. See Honour v. Equitable Life Assurance Society of the United States (1900) 1 Ch. 852, 854; cf. Automotive Equipment Inc. v. Trico Products Corp., 11 F. Supp. 292 (W. D. N. Y., 1935). But cf. Aetna Life Insurance Co. v. Richmond, 107 Conn. 117, 139 Atl. 702 (1927). It is also argued that the declaratory judgment procedure is unsuitable to patent litigation, since as a summary process, it is not adaptable to cases where the facts are complicated, or seriously in dispute. See Rossman, op. cit. *supra* note 14, at 3, 5; Borchard, *The Federal Declaratory Judgment Act* (1934) 21 VA. L. REV. 35, 47. Both these objections, however, are merely appeals to the court's discretion, and have no weight where relief by declaration is the sole remedy available. See BORCHARD, op. cit. *supra* note 13, at 68, 110, 114, 115, 178. See also Part 3 of the Declaratory Judgment Act, 48 STAT. 955, 28 U. S. C. A. § 400 (1934), which provides for reference of issues to a jury, thus indicating legislative recognition of the possibility of complicated issues of fact being tried in a suit for declaratory relief.

24. Stripling and Thomas, *Declaratory Judgments in Patent Cases* (1935) 17 J. PATENT OFFICE SOCIETY 422.

25. Part 1 of the Act confines the issuance of the declaratory judgment to cases of "actual controversy" 48 STAT. 955, 28 U. S. C. A. § 400 (1934). Cf. O'Brien, *Restrictions on the Usefulness of Declaratory Judgment in Patent Suits* (1935) 17 J. PATENT OFFICE SOCIETY 270, 278.

26. It appears evident that the threatened dealer may also have recourse to relief by declaration. The question arises, however, whether a general allegation of infringement would be sufficient to create a controversy between the patentee and all dealers in the product. This issue probably will not be raised since the manufacturer, as the party most interested in obtaining an adjudication, would ordinarily petition immediately for a declaration of non-infringement and assure his dealers that the matter was being settled. See notes 3, 12 and 25 *supra*.

VALIDITY OF SPENDTHRIFT TRUSTS

THOUGH all trusts which are designed to assure the cestui que trust a life interest which cannot be transferred by him nor attached by his creditors are often loosely designated as spendthrift trusts, it is more accurate to classify trusts with this common purpose as discretionary trusts, trusts for support, and the true spendthrift trusts.[1] In the discretionary trust, the settlor protects his cestui by providing that he may receive only so much of the income as the trustee in his absolute discretion sees fit to give him.[2] Though there may be no express prohibition upon seizure by creditors in this type of trust, it has universally been held that creditors cannot attach nor can the cestui alienate since neither can compel the trustee to exercise his discretionary power.[3] Somewhat less discretion is given to the trustee in the trust for support since it is usually provided in such cases that the cestui shall be paid as much of the income as is necessary for his support.[4] Here also voluntary and involuntary alienation is prevented, not necessarily by virtue of express prohibitions but rather because of the indefinite nature of the cestui's interest.[5] While these trusts have been unanimously upheld, a great controversy has arisen concerning the true spendthrift trust, in which the trustee is under an absolute duty to pay a sum certain to the cestui who is protected in the trust agreement solely by express prohibitions against seizure by creditors and against voluntary assignment. The prohibition against seizure by creditors is chiefly responsible for the conflicting views. When the cestui of a trust has an unqualified right to payment, it follows that his creditor would be permitted to attach the payments in the hands of the trustee unless the courts are willing to give effect to the settlor's prohibition upon seizure. Since the legal arguments on the one hand that a creditor may attach each absolute right of his debtor and on the other that a settlor may restrict or regulate the use of his gift, are irreconcilable, the holding of each jurisdiction upon the validity of the spendthrift trust has been based upon its own view as to the trust's social utility.[6] Though most of the American decisions before 1880,

1. See RESTATEMENT, TRUSTS (Tent. Draft, 1931) § 148, 150, 151; 1 BOGERT, TRUSTS AND TRUSTEES (1935) § 226.

2. Funk v. Grulke et al., 204 Iowa 314, 213 N. W. 608 (1927); Brown v. Lumbert, 221 Mass. 419, 108 N. E. 1079 (1915); Wolfman v. Webster et al., 77 N. H. 24, 86 Atl. 259 (1913).

3. Foley v. Hastings, 107 Conn. 9, 139 Atl. 305 (1927); In re Baeder's Estate, 190 Pa. 614, 42 Atl. 1104 (1899); see RESTATEMENT, TRUSTS (Tent. Draft, 1931) § 151.

4. Baker v. Brown et al., 146 Mass. 369, 15 N. E. 783 (1888); Abbott v. Abbott et al., 76 N. H. 225, 81 Atl. 699 (1911); Barnes v. Dow, 59 Vt. 530, 10 Atl. 258 (1887).

5. Parker, Holmes & Co. v. Bushnell, 80 Conn. 233, 67 Atl. 479 (1907); Meek v. Briggs et al., 87 Iowa 610, 54 N. W. 456 (1893); Mitchell et al. v. Choctaw Bank, 107 Miss. 314, 65 So. 278 (1914); see RESTATEMENT, TRUSTS (Tent. Draft, 1931) § 150.

6. "That it shall be alienable by and subject to the debts of its beneficial owner is not an essential element of any estate . . . in the sense that it is a logical impossibility for such an estate to exist without these incidents. Wherever it is held that such provisions are invalid, upon final analysis it will be found that the true reason for the holding is not that such provisions are repugnant to or inconsistent with the estate granted or given, but that it is deemed to be against public policy as it is declared by the common and/or statute law to permit them to be attached to the estate in question." Epes, J. in Sheridan v. Krause, 161 Va. 873, 893, 172 S. E. 508, 514 (1934).

On the one hand it is argued that the spendthrift trust is pernicious because it encourages the accumulation of fortunes in single hands, protects the able-bodied in most instances, takes property out of commerce, and permits the evasion of just debts. On the other hand it is contended that since the property settled belongs to the settlor, he should be allowed to dictate the manner in which it is to be used, especially since the spendthrift trust profollowing the English decisions, invalidated attempted spendthrift trusts,[7] the trend since that time in the United States has been sharply toward recognition, until today the great majority of American courts uphold them.[8]

In a recent decision,[9] the New Hampshire supreme court, ruling for the first time on the validity of the spendthrift trust, disregarded the great weight of authority, and became the first jurisdiction since Gray's classic denunciation of spendthrift trusts to follow his views.[10] Settlor gave property to a trustee with instructions to pay to the cestui que trust $5000 annually out of the net income of the trust, and with the further provision that the income ". . . shall not be assigned, alienated or pledged in any manner, or be subject to attachment or any indebtedness . . ." of the cestui. A judgment creditor of the cestui brought a creditor's bill, seeking to charge the cestui's right to payment from the annuity. The court held that, since the cestui's absolute right to payment from the trust was a "credit" within the meaning of the trustee process statute which provided that all "credits" of the beneficiary in the trustee's possession could be attached, the provision against seizure was void and consequently that the annuity was attachable. Though a discussion of the prohibition upon voluntary alienation was not necessary to a disposition of this case, the court further indicated that this prohibition would probably be held valid should this question be litigated. Since in practically all instances courts have treated both types of restraint as necessarily complimentary,[11] the instant decision is unique in holding that the restraint on

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tects the weak and improvident. In addition, it is argued in favor of the spendthrift trust that it neither deceives creditors, since public records and credit ratings are available, nor ties up property unduly nor tends to accumulate fortunes, since the trust is but for a lifetime and since its purpose is not enlargement of the trust estate. See Nichols, Assignee v. Eaton et al., 91 U. S. 716, 726 (1875); 2 BOGERT, TRUSTS AND TRUSTEES (1935) § 222; GRAY, RESTRAINTS ON THE ALIENATION OF PROPERTY (2d ed. 1895) vi; Brown, *Spendthrift Trusts* (1902) 54 CENT. L. J. 382, 387; Costigan, *Spendthrift Trusts Reexamined* (1934) 22 CAL. L. REV. 471, 483, 487, 489, 497.

7. GRAY, op. cit. *supra* note 6, at 169.

8. 1 BOGERT, TRUSTS AND TRUSTEES 723; see Runk, *Modifications of the Rule Against Perpetuities* (1932) 80 U. OF PA. L. REV. 397, 405; Comment (1931) 29 MICH. L. REV. 493; (1935) 44 YALE L. J. 1116, 1117.

9. Brahmey v. Rollins et al., 179 Atl. 186 (N. H. 1935).

10. See LEACH, CASES & MATERIALS ON THE LAW OF FUTURE INTERESTS (1935) 963.

11. Courts have uniformly treated the two prohibitions as complimentary. Hence when a trust instrument which contains but one of the prohibitions is construed by a court, the missing provision is usually implied. Prohibition against seizure implied from presence of prohibition on voluntary alienation: Steib v. Whitehead, 111 Ill. 247 (1884); Jouvenat v. Continental Nat'l Bk., 253 Ill. App. 400 (1929); Partridge v. Cavender, 96 Mo. 452, 9 S. W. 785 (1888); Matthews v. Van Cleve, 282 Mo. 19, 221 S. W. 34 (1920); Winthrop Co. v. Clinton, 196 Pa. 472, 46 Atl. 435 (1900); White v. O'Bryan, 148 Tenn. 18, 251 S. W. 785 (1923); see Jones v. Harrison, 7 F. (2d) 461, 465 (C. C. A. 8th, 1925); RESTATEMENT, TRUSTS (Tent. Draft, 1931) § 148; (1933) 81 U. OF PA. L. REV. 480. Prohibition against voluntary alienation implied from presence of prohibition against seizure: Commissioner of Int. Rev. v. Blair, 60 F. (2d) 340 (C. C. A. 7th, 1932); Shankland's Appeal, 47 Pa. 113 (1864); see Jones v. Harrison, *supra*, at 465; RESTATEMENT, TRUSTS, *supra* at § 148; (1933) 81 U. OF PA. L. REV. 480. *Contra:* Ames v. Clark, 106 Mass. 573 (1871); Boston Safe Deposit & Trust Co. v. Luke, 220 Mass. 484, 108 N. E. 64 (1915); but see Eaton v. Boston Safe Deposit & Trust Co., 240 U. S. 427 (1916); Griswold, *Beneficiary of Spendthrift Trust* (1929) 43 HARV. L. REV. 63, 77. On the other hand, the desire of the courts to treat the two prohibitions as complimentary often has resulted in the holding that since a single prohibition is not enough to create a spendthrift trust, the single prohibition is void. Single prohibition against seizure

seizure may be invalidated without destroying the restraint on alienation. This distinction between the two types of restraints was justified on the ground that, while the right to alienate is an element of ownership which a donor may withhold, on the other hand the right of creditors to seize is a right of third parties conferred by law and not subject to any power of the donor to withhold or grant. Further, such a distinction was held more equitably to balance the interests of creditors and cestuis, since the restraint on alienation protects the cestui somewhat, without prejudicing his creditors as does the restraint on seizure.

While such a balancing of the interests of creditors and cestuis has been effected in ten jurisdictions through spendthrift trust statutes whereby creditors are allowed to reach the surplus funds of the trust which are not needed by the beneficiary for his support,[12] it is questionable whether the instant device of distinguishing between prohibitions on seizure and alienation leaves any real protection to the cestui of the spendthrift trust. For, while the restraint on alienation prevents the cestui from assigning his future interest in the income, nevertheless, since the creditor ordinarily can levy upon the future rights to payment from the trust income,[13] the cestui, by going so heavily into debt that his debts exceed the total income from the trust, can lose all benefit from the funds through creditors' suits. Indeed, the only practical effect of the distinction made by the New Hampshire court seems to be to further protect creditors to the extent that the restraint on alienation may tend to prevent preferential assignments of income by the debtor. In reality, therefore, the decision appears to nullify the purpose of the spendthrift trust, thus affording a precedent to those seeking new weapons in the attack on the present American rule validating spendthrift trusts.

POWER OF FEDERAL COURTS TO DIRECT A JUDGMENT CONTRARY TO VERDICT OF JURY

AT COMMON law, when the pleadings presented no material issue of fact, but a verdict of the jury was nevertheless taken, that verdict could be disregarded by the trial or appellate court, and judgment directed according to the state of the pleadings.[1] Thus, if the defendant confessed the plaintiff's allegations, and plead, by way of defense, facts which would not constitute a bar even if true, a judgment non obstante verdicto might be entered for plaintiff even though the jury rendered a verdict for the defendant.[2] Or if plaintiff's allegations, even if true, would not entitle him as a matter of law to recover, a jury verdict for the plaintiff might be set aside and judgment directed for the defendant upon motion to arrest judgment on the verdict.[3] Where, however, the pleadings presented a material issue of fact and the jury returned a ver-

void: Croom v. Ocala Plumbing & Electric Co., 62 Fla. 460, 57 So. 243 (1911); Ullman v. Cameron, 186 N. Y. 339, 78 N. E. 1074 (1906); In re Morgan's Estate, 223 Pa. 228, 72 Atl. 498 (1909); see Bergmann v. Lord, 194 N. Y. 70, 75, 86 N. E. 828, 830 (1909). Single prohibition against voluntary alienation void: Newcomb v. Masters, 287 Ill. 26, 122 N. E. 85 (1919).

12. See 2 POWELL, CASES ON TRUSTS AND ESTATES (1933) 859 n.

13. Hamilton v. Drogo, 241 N. Y. 401, 150 N. E. 496 (1926); see 1 BOGERT, TRUSTS AND TRUSTEES § 193.

1. SMITH, AN ACTION AT LAW (3d London ed. 1848) 161.

2. United States v. Gardner, 133 Fed. 285 (C. C. A. 9th, 1904); Bradshaw v. Hedge & Heaton, 10 Iowa 402 (1860); Burdick v. Green, 18 Johns. 14 (N. Y. 1820); Cook v. Pearce, 8 Q. B. 1044 (1843); Atkinson v. Davies, 11 M. & W. 236 (Ex. 1843).

3. Bartlett v. Crozier, 17 Johns. 439 (N. Y. 1820); Phelps v. Baldwin, 17 Conn. 209 (1845); Harbin v. Hunt, 151 Ga. 60, 105 S. E. 842 (1921).

dict for the plaintiff, the Supreme Court held in *Slocum v. New York Life Insurance Co.*[4] that neither the trial court nor the appellate court could thereafter direct a verdict for the defendant on the ground that the evidence was insufficient to support the jury's verdict, but must order a new trial.[5] The basis of the holding was that, when the court rejects the jury's findings of fact, it at the same time reopens the issues of fact and can enter a judgment contrary to that of the jury only by itself determining those issues, which is contrary to the Seventh Amendment.[6]

That decision was not binding on state courts, since it was merely an interpretation of the Seventh Amendment, which is a restriction only upon the federal government.[7] And since a necessary consequence of adherence to the *Slocum* decision would be prolonged litigation, most states have refused to follow it. Some courts have placed their decisions on the ground that their state constitutions merely provide that trial by jury shall remain inviolate, rather than that "no fact tried by the jury shall be otherwise re-examined . . . than according to the rules of the common law," as does the Seventh Amendment.[8] Other state courts have declined to follow the *Slocum* case on the ground that it was an incorrect interpretation of the common law.[9] While federal courts were bound by the decision, efforts were soon made to escape the effect of the ruling by resort to the common law method of reservation by the court of decision upon a question of law until after the jury had rendered its verdict.[10] By this method the trial or appellate courts could set aside a verdict of the jury and direct judgment according to the question of law taken under reservation.[11]

This device was attempted in the recent case of *Baltimore & Carolina Line, Inc. v. Donald Redman.*[12] Defendant, at the conclusion of the presentation of evidence, moved for a directed verdict and a dismissal of the complaint on the ground that the evidence was insufficient to sustain a verdict for the plaintiff. The court reserved decision on these motions and submitted the case to the jury, who returned a verdict for the plaintiff. Thereafter the court denied the defendant's motions and accordingly

4. 228 U. S. 364 (1913).

5. This case has been severely criticized. See Thayer, *Judicial Administration* (1915) 63 U. OF PA. L. REV. 585; Scott, *Trial by Jury and the Reform of Civil Procedure* (1918) 31 HARV. L. REV. 669; *Comment* (1914) 23 YALE L. J. 454; Note (1913) 47 AM. L. REV. 906; Note (1914) 26 GREEN BAG 106. But see Schofield, *New Trials and the Seventh Amendment* (1913-1914) 8 ILL. L. REV. 287, 381, 465.

6. The Seventh Amendment provides, "In suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury shall be otherwise re-examined in any court of the United States, than according to the rules of the common law."

7. Edwards v. Elliott, 88 U. S. 532 (1874); Walker v. Sauvinet, 92 U. S. 90 (1875); Pearson v. Yewdall, 95 U. S. 294 (1877).

8. Bothwell v. Boston Elevated Ry. Co., 215 Mass. 467, 102 N. E. 665 (1913); Gulf & Ship Island Rr. Co. v. Hales, 140 Miss. 829, 105 So. 458 (1925); 2 THOMPSON, TRIALS (2d ed. 1912) 1478 (collection of the various constitutional provisions).

9. Wayland v. Latham, 89 Cal. App. 55, 264 Pac. 766 (1928); Vandenburg v. Kaat, 252 Mich. 187, 233 N. W. 220 (1930).

10. Hoffman v. American Mills Co., 288 Fed. 768 (C. C. A. 2d, 1923); Italian Star Line, Inc. v. United States Shipping Board Emergency Fleet Corp., 53 F. (2d) 359 (C. C. A. 2d, 1931); see Clemence v. Hudson & Manhattan Ry. Co., 11 F. (2d) 913, 917 (C. C. A. 2d, 1926); Bohenik v. Delaware & Hudson Co., 49 F. (2d) 722, 724 (C. C. A. 2d, 1931).

11. Carleton v. Griffin, 1 Burrows Rep. 549 (K. B. 1758); Dublin, Wicklow, & Wexford Railway Co. v. Slattery, 3 App. Cas. 1155 (1878); see 3 BL. COMM. (Lewis ed. 1897) 378; THAYER, PRELIMINARY TREATISE ON EVIDENCE (1898) 240.

12. 55 Sup. Ct. 890 (1935).

entered judgment for the plaintiff. Upon appeal, the circuit court of appeals held the evidence insufficient to support a verdict for plaintiff, but believing the *Slocum* case controlling precedent, ordered a new trial, rather than direct a verdict for defendant.[13] Upon certiorari to the Supreme Court, it was held that since the trial court had reserved decision on the motions of defendant, the circuit court upon a finding of insufficiency of evidence should have directed a proper judgment rather than remit the case for a new trial. The court based its decision on the fact that at common law a court could direct a verdict for one party despite a jury verdict for the other, when the court had reserved decision on a question of law relative to the suit. Since such a procedure was proper at common law, its use by the federal court was held not violative of the Seventh Amendment.[14] The *Slocum* case was distinguished solely upon the ground that there the court had made no reservation of power to grant or deny, subsequent to the jury verdict, a motion for a directed verdict.

Apparently the distinction between the case where there had been a reservation and where there had not been was based on the common law theory that, in the case where a reservation had been taken, the jury consented to allow the court's ultimate ruling on the question of law to be a part of its verdict. Accordingly, when the court finally decided as a matter of law that there was insufficient evidence to support a verdict for the plaintiff, and that judgment should therefore have been entered for the defendant, a direction to that effect would not mean that the jury's verdict had been overruled, or the province of the jury invaded, for it had consented to such a judgment being entered. While at an early date the express consent of the jury may have been obtained, subsequently that consent was merely presumed, and it apparently lay solely within the court's discretion to reserve decision upon a question of law, or not.[15] Actually, therefore, there seems to be no practical difference between the case where there has been and where there has not been a reservation of power by the court. In either case, the court is answering the same question of law, that is, whether there is sufficient evidence to support a verdict for the plaintiff, and granting or denying the motion accordingly. The degree of interference with the jury's function, if any, in each case is obviously the same. Hence, the distinction between the two cases is reduced to a mere question of form.

It seems clear that the distinction which affords a means of reconciling the *Slocum* and the present case was seized upon by the Court so as to avert the effects of the former case without directly overruling it. Insofar as that purpose is accomplished, the decision may be hailed as a salutary one. Nevertheless, it does leave open an opportunity for needless trials, when a trial judge inadvertently fails to reserve his decision on a question of law. Moreover, it raises questions as to what shall constitute a proper reservation. In the instant case, the court mentions the fact that plaintiff's counsel made no objection to the reservation by the court. From this, it may be implied that, if plaintiff had made such objection, the result may have been different. While the weight of authority seems to hold that the reservation of a question of law is taken with the tacit consent of the jury only, and not that of counsel,[15] it has forcefully been contended that the parties' consent is needed to reserve a question of law.[16] In any event, the result of the instant case is to leave the matter unsettled as yet in the federal courts.[17] Finally, it seems as undesirable to require a new trial when there has

13. Donald Redman v. Baltimore & Caroline Line, Inc., 70 F. (2d) 635 (C. C. A. 2d, 1934).

14. Capital Traction Co. v. Hof, 174 U. S. 1 (1899).

15. See Thayer, *supra* note 5, at 601; Scott, *supra* note 5, at 685; Note (1913) 47 AM. L. REV. 906, 908; Note (1914) 26 GREEN BAG 106, 112; 2 TIDD, PRACTICE (2d Am. ed. 1828) 931.

16. See Schofield, *supra* note 5.

17. A state court has found it to be at the discretion of the court. Blyth v. Quinby &

been no reservation as when there has been one. It would appear that, in the interests of simplifying and speeding up federal procedure, an overruling of the *Slocum* case would be preferable to the result of the instant case.

PROCESS PATENT PROTECTION BY EXCLUSION OF FOREIGN PRODUCTS UNDER TARIFF ACT

THE defendant Amtorg Trading Corporation sought to import into this country six thousand tons of phosphate, an unpatented product produced in Russia by a flotation process which was protected in this country by a United States process patent. The licensees of the owner of the patent, remediless under the patent law which operates only "within the United States, and the Territories thereof,"[1] complained to the United States Tariff Commission that the foreign use of the patented process, and the importation and sale of the product, was unlawful under section 337 of the Tariff Act of 1930 as an unfair method of competition and unfair act.[2] The Tariff Commission, finding that the patented process had been used, held, in accordance with a prior holding of the Court of Customs and Patents Appeals,[3] that the importation of the phosphate was unlawful. A presidential order of exclusion then issued, as provided by section 337. On appeal the Court of Customs and Patents Appeals, distinguishing one of its prior decisions and expressly overruling another in part,[4] reversed the Commission's decision.[5] The court distinguished between the importation of patented products, to which the Act admittedly applied, and of unpatented products made abroad by a patented process, on the ground that the unauthorized sale in this

Co., 148 App. Div. 871, 133 N. Y. Supp. 602 (1st Dep't, 1912); Kagan v. Avallone, 243 App. Div. 437, 277 N. Y. Supp. 837 (1st Dep't, 1935).

1. A United States patent is "a grant to the patentee, his heirs or assigns, for the term of seventeen years, of the exclusive right to make, use and vend the invention or discovery throughout the United States and the Territories thereof." 16 STAT. 201 (1870), 35 U. S. C. A. § 40 (1926).

2. 46 STAT. 703 (1930), 19 U. S. C. A. § 1337 (1934). Subsection (a) of the act reads: "Unfair methods of competition and unfair acts in the importation of articles into the United States, or in their sale by the owner, importer, consignee, or agent of either, the effect or tendency of which is to destroy or substantially injure an industry, efficiently and economically operated, in the United States, or to prevent the establishment of such an industry, or to restrain or monopolize trade and commerce in the United States, are hereby declared unlawful. . . ." And subsection (e) provides: "Whenever the existence of any such unfair method or act shall be established to the satisfaction of the President he shall direct that the articles concerned in such unfair methods or acts, shall be excluded from entry into the United States. . . ."

3. Frischer & Co., Inc. v. Bakelite Corp., 39 F. (2d) 247 (C. C. P. A. 1930), cert. denied, 282 U. S. 852 (1930); Comment (1930) 40 YALE L. J. 108.

4. Frischer & Co., Inc. v. Bakelite Corp., *supra* note 3, was distinguished as involving only a product patent. The patent concerned, however, was ambiguous and had been interpreted by the Tariff Commission as covering the process. The case of In re Northern Pigment Co., 71 F. (2d) 447 (C. C. P. A. 1934), noted in (1934) 3 GEO. WASH. L. REV. 224, involving both product and process claims, was overruled insofar as it held that the importation of an unpatented product made by the unauthorized use of the process was unfair. The section has been applied in only one other patent case. In re Orion Co., 71 F. (2d) 458 (C. C. P. A. 1934) (product claim).

5. In re Amtorg Trading Corp., 75 F. (2d) 826 (C. C. P. A. 1935), Bland, J., dissenting. Certiorari denied for want of jurisdiction under the Tariff Act, sub. nom. International Agricultural Credit Corp. v. Amtorg Trading Corp., U. S. L. Week, Oct. 15, 1935, at 91.

country of the former was a violation of the patent laws, and therefore their importation was unfair within the meaning of the Tariff Act, whereas the unauthorized sale here of the latter was lawful under the patent laws, and therefore the importation of such articles was not unfair under the Tariff Act.

Under the patent laws the courts have drawn a distinction between the extent of the monopoly conferred by a product patent and that granted by a process patent. Since a product patent grants the exclusive right to make, use and vend the patented product, the sale of that product is an infringement. But a process patent grants such right only as to the patented process, and consequently, the sale of the product made by the infringing use of the process is not an infringement.[6] In domestic commerce this rule is justified since the process patentee is amply protected by a right of action against the infringing manufacturer,[7] and to grant him an additional right of action against each vendor would unnecessarily hamper trade[8] and encourage multiplicity of actions. On the other hand, when the patented process is used in a foreign country, and the resulting unpatented product imported, the patentee has no right of action against the manufacturer who is beyond the territorial limits of this country,[9] and he is unprotected unless permitted to bring an infringement action against the importer or vendor of the product. To deny him this remedy, therefore, is to nullify the value of his patent monopoly to the extent that products made by the foreign use of the process are sold in the American market. The obvious effect is not only to lessen the incentive to invention given by the patent laws, but also to promote the secret use of new processes in those industries in which foreign competitors appear likely to benefit from the disclosure of the process through registration of the patent.[10] An indirect result of the process patentee's lack of remedy is that those American producers who are denied the use of the process are placed at a disadvantage in the domestic as well as the foreign market, since they must compete with foreign manufacturers who enjoy the economic advantage of the improved process without cost. They are thereby encouraged to evade the patent laws themselves simply by moving their factories across the border and importing the product.[11]

Although the threat of loss to American process patentees from this source has not been sufficient to evoke much agitation for patent law reform,[12] nevertheless with the

6. Simpson v. Wilson, 44 U. S. 709 (1846); Merrill v. Yeomans, 94 U. S. 568 (1876); Goodyear v. N. J. Central Rr. Co., 10 Fed. Cas. 664 (C. C. N. J. 1853); see Barton v. Nevada Consolidated Copper Co., 36 F. (2d) 85 (S. D. N. Y. 1929) and cases cited. But cf. Fulton Co. v. Bishop & Babcock Co., 17 F. (2d) 1006 (C. C. A. 6th, 1927); Warner v. Tennessee Products Corp., 57 F. (2d) 642 (C. C. A. 6th, 1932)

7. Welsbach Light Co. v. Union Incandescent Light Co., 101 Fed. 131 (C. C. A. 2d, 1900).

8. See Goodyear v. N. J. Central Rr. Co., 10 Fed. Cas. 664 at 668 (C. C. N. J. 1853).

9. "Infringement cannot be predicated of acts wholly done in a foreign country." Dowagiac Mfg. Co. v. Minnesota Moline Plow Co., 235 U. S. 641, 650 (1915) (patented products sold in Canada); Bullock Elec. & Mfg. Co. v. Westinghouse Elec. & Mfg. Co., 129 Fed. 105 (C. C. A. 6th, 1904); Rushmore v. Manhattan Screw & Stamping Works, 170 Fed. 188 (C. C. S. D. N. Y. 1909); see Victor Talking Machine Co. v. Strauss, 171 Fed. 673, at 673 (C. C. S. D. N. Y. 1909).

10. See Pennock v. Dialogue, 27 U. S. 1, 19 (1829).

11. This occurred in In re Northern Pigment Co., 71 F. (2d) 447 (C. C. P. A. 1934) and the court sustained the finding of the Tariff Commission that this was unfair within the meaning of the Act. That case was expressly overruled as to this point by the decision in the principal case.

12. See Report of the Committee on Patent Law Revision of the American Bar Association (1934) 16 J. PATENT OFFICE SOCIETY 731, 736; Boyle, *The Product of the Process*

development throughout the world of modern industrial technique, particularly in those countries with low costs of production, this threat will tend to increase. A number of countries, particularly those so situated geographically as to be open to foreign competition, have found it necessary to afford the process patentee protection by extending the patent monopoly for a process to cover the product.[13] While in some cases the American patentee may be able to protect himself by obtaining foreign patent protection for his process,[14] nevertheless, particularly when the patentee is a small manufacturer, the financial and technical difficulties of obtaining a foreign patent may make this means of protection impracticable.[15] Again, in a few cases the American patentee may be able to secure American patent protection for both his process and its product, but this is usually unavailable since it will be granted only when both the process and the product involve new discoveries.[16] A third possibility is the extension of the patent laws by statutory amendment. Since the problem involves broad questions of legislative policy, this latter method suggests itself as the most satisfactory one.[17] Presumably if this method were adopted, the process patentee would, under the rationale of the instant case, be entitled to the additional remedy of exclusion of the unpatented product under the Tariff Act. A fourth method of protecting the process patent monopoly is by excluding the foreign-made product on the ground that the unauthorized use of the patented process abroad and the importation of the product, though lawful under the patent laws, is an unfair method of competition or unfair act in the importation of articles under the Tariff Act.

In reaching its conclusion that the foreign use of the patented process and the importation of the unpatented product did not come within the scope of the Act, the court assumed that Congress, when it used the words "unfair methods of competition," intended them to have the same meaning in regard to competition between domestic and foreign competitors as the same words, used in the Federal Trade Commission Act, have had in relation to competition between domestic business men.[18] The test commonly applied under the latter Act has been whether or not the practices involved were opposed to good morals, characterized by deception, or against public

(1933) 15 J. PATENT OFFICE SOCIETY 192. Presumably process patentees have been protected since 1930 under the decision in the *Frischer* case, *supra* note 3.

13. The English courts, under a statute similar to the patent act in this country, hold that the importation and sale in England of articles manufactured in another country by a process patented in England is an infringement of the patent. Elmslie v. Boursier, L. R. 9 Eq. 217 (1869); TERRELL, PATENTS (8th ed. 1934) 173. This holding was found necessary to protect "the whole profit, benefit, commodity, and advantage" granted by the patent, and authority supporting the United States rule was disregarded. See HINDMARCH, PATENTS (1847) at 302; 14 SOL. J. 690 (1870). In the following countries also a patent for a process extends to the product: Bulgaria, Czechoslovakia, Danzig, Denmark, Germany, Greece, Hungary, Japan, the Netherlands, and Poland. See LADAS, THE INTERNATIONAL PROTECTION OF INDUSTRIAL PROPERTY, (1930) 244.

14. Report of Committee on Patent Law Revision of the American Bar Association, *supra* note 12, at 737; Brown, *Is Patent Protection Abroad Advisable?* (1933) 15 J. PATENT OFFICE SOCIETY 115; VAUGHN, ECONOMICS OF OUR PATENT SYSTEM (1925) 245.

15. For the difficulties which existed prior to the establishment of the International Union for the Protection of Industrial Property, see LADAS, op. cit. *supra* note 13, at 31-32. And for the efforts to remedy the problems and the present status, see LADAS, chs. 9-13.

16. See P. E. Sharpless Co. v. Crawford Farms, 287 Fed. 655 at 656 (C. C. A. 2d, 1923).

17. See Report of the Committee on Patent Law Revision of the American Bar Association, *supra* note 12, at 736.

18. The Tariff Commission at first supported this view. See 6th ANNUAL REPORT OF THE U. S. TARIFF COMMISSION (1922) 4.

policy as tending to create monopoly.[19] The court felt that the importation and sale of the phosphate under the circumstances of the instant case could not be included within this test. Section 337, however, does not require such a limited interpretation, for the words used are broader than those in the Federal Trade Commission Act,[20] and could easily have been construed to cover the present practices. Furthermore, the legislative history of the section indicates that Congress has approved its use to protect the interests of process patentees. The present provision first appeared as section 316 of the Tariff Act of 1922, and under that Act the Tariff Commission made its finding, upheld in the *Frischer* case,[3] that the foreign use of the patented process and the importation of the product was an unfair method of competition or unfair act within the scope of the section. During the consideration of the Tariff Act of 1930, the Commission called the attention of the Ways and Means Committee of the House to this finding and recommended that section 316 be reenacted as the sole protection available to process patentees under the law.[21] When Congress reenacted the section as section 337 of the 1930 Act it thereby presumably adopted the construction placed on the wording by the Tariff Commission.[22]

ESTATE TAXATION OF PROPERTY SUBJECT TO A GENERAL TESTAMENTARY POWER OF APPOINTMENT

DONOR'S will gave donee a life estate, and a general testamentary power of appointment to dispose of the remainder in fee. It further provided that in default of donee's exercise of her power, the remainder should go to designated remaindermen. After donor's death, but before the exercise of the power by donee, the Federal Estate Tax statute was enacted, section 302 (f) of which included in taxable gross estate all property ". . . passing under a general power of appointment exercised by decedent."[1] Donee exercised her power in favor of donor's remaindermen, who would have taken had donee not exercised her power, but donor's remaindermen renounced the remainder under donee's appointment and elected to succeed under the provisions of donor's will. In refusing to uphold the tax commissioner's contention that the remainder was taxable as part of donee's gross estate, the United States Supreme Court held that since donor's remainderman had not been divested by donee, and in addition had

19. Federal Trade Commission v. Gratz, 253 U. S. 421 (1920).

20. The section declares unlawful not only "unfair methods of competition" but "unfair acts in the importation." Furthermore, it seems broader in purpose than the Federal Trade Commission Act, being directed at practices "the effect of which is to destroy or substantially injure an industry, efficiently and economically operated, in the United States." *Supra* note 2. The Senate Finance Committee, in reporting the section to the Senate, said: "The provision relating to unfair methods of competition in the importation of goods is broad enough to prevent every type and form of unfair practice and is, therefore, a more adequate protection to American industry than any anti-dumping statute the country ever had." SEN. REP. No. 595, 67th Cong., 2nd Sess. (1922) 3.

21. Vol. 17, Supp. to Tariff Readjustment Reports on Tariff Bill of 1929, p. 10667.

22. See U. S. v. Bailey, 34 U. S. 238, 256 (1835); Hecht v. Malley, 265 U. S. 144 (1924) and cases cited. Unfortunately, the holding in the Frischer case was ambiguous, and the majority of the court in the principal case felt that it did not concern *process* patents, but only product patents.

1. Revenue Act of 1926, c. 27, § 302(f), 44 STAT. 70, 26 U. S. C. A. § 1094(f) (1926), 26 U. S. C. A. § 411(f) (1935).

A general testamentary power of appointment is a general power under the statute. Whitlock-Rose v. McCaughn, 21 F. (2d) 164 (C. C. A. 3d, 1927).

elected to succeed from donor, the property did not "pass" from donee under the exercise of her power.[2]

The Federal Estate Tax statute[1] and almost all the state inheritance tax statutes[3] contain provisions for the taxation of property subject to a general power of appointment.[4] Under these statutes, there seems to be little doubt that a transfer, taxable as coming from donee, results when donee exercises his power in favor of his own appointee, divesting donor's remainderman.[5] The real point of controversy is that involved in the principal case, namely, whether for purposes of succession taxation the remainder shall be deemed to have been transferred from donor or from donee when donee exercises his power of appointment in favor of donor's remainderman; whether, in other words, the exercise of the power by donee should be considered a superfluous act, or should be regarded as sufficiently instrumental in the transfer of the property to warrant the imposition of a tax. This question is often raised under the state inheritance tax statutes for the purpose of contesting the tax on the ground that it is retroactive and therefore unconstitutional. For where the tax statute was enacted after the death of the donor, a tax on donor's remainderman would be retroactive if it is held that the remainder passed from donor and not from donee.[6] Under the Federal Estate Tax statute the question is not one of retroactivity but whether, even if the donor's estate was taxed at donor's death, the property may be taxed again to the estate of the donee at donee's death. For if the remainder is held to have come from donor, there can be no tax to donee's estate.[7] Under both the state and federal statutes the courts have split on the question whether a transfer from the donee occurs in the case mentioned.

In state inheritance taxation, where the conflict originated, one group of states follows the New York rule[8] which adheres to the common law doctrine that donor's remainderman takes a vested remainder, subject to divestment, from donor. From

2. Helvering v. Grinnell, 294 U. S. 153 (1935), aff'g 70 F. (2d) 705 (C. C. A. 2d, 1934), rev'g 28 B. T. A. 1346 (1933).

3. For a collection of state statutes, see GLEASON AND OTIS, INHERITANCE TAXATION (4th ed. 1925) 968 et seq.; PINKERTON AND MILLSAPS, INHERITANCE AND ESTATE TAXES (1926) 531 et seq.

4. In the absence of specific statutory provision, there is no taxable transfer from donee under state inheritance tax statutes or the Federal Estate Tax Act, since it is the common law rule that donee's appointee succeeds from donor and not from donee. SUGDEN, POWERS (8th ed. 1861) 470; 4 KENT COMM. (Text Book Series 1889) 337, 338. United States v. Field, 255 U. S. 257 (1921); Emmons v. Shaw, 171 Mass. 410, 50 N. E. 1033 (1898).

5. Orr v. Gilman, 183 U. S. 278 (1901); Stratton v. United States, 50 F. (2d) 48 (C. C. A. 1st, 1931), cert. denied, 284 U. S. 651 (1931).

6. Matter of Slosson, 216 N. Y. 79, 110 N. E. 166 (1915); Matter of Harbeck, 161 N. Y. 211, 55 N. E. 850 (1900) (before specific power of appointment provision was included in the statute). See notes 8 and 9, *infra*.

7. United States v. Field, 255 U. S. 257 (1921); Lederer v. Pearce, 266 Fed. 497 (C. C. A. 3d, 1920). Both decisions were rendered before specific power of appointment provision was included in the federal statute. See note 13, *infra*.

8. Matter of Lansing, 182 N. Y. 238, 74 N. E. 882 (1905). Despite a broadly worded statute which provided that a taxable transfer occurred from donee whether he exercised his power or not, the New York Court of Appeals refused to permit a tax to donor's remainderman either when donee specifically appointed him, or allowed the remainder to pass to him by a non-exercise of his power of appointment. Id. at 248, 249, 74 N. E. at 885. The statute was later changed to permit a tax only when donee exercised his power. New York Sess. Laws, 1911, c. 732. For the interpretation given this amended statute, see GLEASON AND OTIS, op. cit. *supra* note 3, at 351.

this premise, it follows that donee's exercise of his power in favor of donor's remainderman is an ineffectual attempt to transfer to donor's remainderman an estate which he already possesses. Thus an inheritance tax upon donor's remainderman for an estate which was transferred to him by donor's will before a taxing statute was enacted is retroactive and unconstitutional.[9] Another group of states follows the Massachusetts rule[10] which holds, contrary to the common law doctrine, that the succession to the remainder is held in abeyance until donee's death. From this premise it is reasoned that donee is an intermediate step in the devolution of the remainder, so that either an exercise or a non-exercise of his power may transfer the remainder to donor's remainderman. Since this transfer occurred after the tax statute was enacted, an inheritance tax to donor's remainderman may be validly imposed.[11] An identical split of authority occurred in the lower federal courts, up to the time of the instant Supreme Court decision, turning upon the interpretation of the ambiguous clause in question in the Federal Estate Tax Act.[12] One group of courts followed the New York rationale and refused to impose a tax upon donee's estate for the value of the remainder when donee appointed donor's remainderman;[13] another group in effect followed the Massachusetts doctrine and taxed donee's estate because donee transferred "economic benefits."[14] In settling the conflict in the federal courts, the principal case expressly adopts the New York "vested remainder" rationale with its consequence that the original transfer by donor must be set aside by donee before a taxable transfer could result from donee under his power. Although it recognized

9. Arkansas, Indiana, Iowa, and Mississippi have adopted statutes similar to the amended New York statute. California, Illinois, Kentucky, and Kansas have enacted the original broad statute, but the courts follow the New York rule. In re Murphy's Estate, 182 Cal. 740, 190 Pac. 46 (1920); State of Kansas v. United States Trust Co. of New York, 99 Kan. 841, 163 Pac. 156 (1917); see Winn v. Schenck, 33 Ky. L. Rep. 615, 617, 110 S. W. 827, 828 (1908); Bentley, *Inheritance Taxation of Powers of Appointment* (1929) 23 ILL. L. REV. 446, 458.

10. Minot v. Stevens, 207 Mass. 588, 93 N. E. 973, 33 L. R. A. (N. S.) 236 (1911). The Supreme Judicial Court held its statute constitutional which provided for a taxable transfer from donee whether he exercised his power of appointment or not.

11. A majority of the states have adopted this liberal statute, and Minnesota and Wisconsin have adopted the Massachusetts rationale in interpreting it. State v. Mary Brooks, 181 Minn. 262, 232 N. W. 331 (1930); Montague v. State, 163 Wis. 58, 157 N. W. 508 (1916). For the Pennsylvania interpretation, see GLEASON AND OTIS, op. cit. *supra* note 3, at 347.

12. The word "passing" in that clause is left open to judicial determination. The present split of interpretation has its source in the ambiguous provision of the Estate Tax Act of 1916, 39 STAT. 777, § 202a, which included in taxable gross estate all property in which decedent had an "interest." The federal courts felt themselves bound by the state court determinations as to whether a power of appointment was an interest in property. See Lederer v. Pearce, 266 Fed. 497, 499 (C. C. A. 3d, 1920). With the adoption of the more specific provisions of § 402(e) of the 1919 Act and § 302(f) of the 1924 Act, the federal courts made an independent interpretation, and abandoned the conflicting state determinations. Fidelity-Philadelphia Trust Co. v. McCaughn, 34 F. (2d) 600, 602, 603 (C. C. A. 3rd, 1929). The original rationales, however, were carried over.

13. Grinnell v. Commissioner of Internal Revenue, 70 F. (2d) 705 (C. C. A. 2d, 1934); Union and Peoples National Bank of Jackson, 30 B. T. A. 1277 (1934); Estate of Helen M. W. Grant, 13 B. T. A. 174 (1928).

14. Lee v. Commissioner of Internal Revenue, 57 F. (2d) 399 (App. D. C. 1932), cert. denied, 286 U. S. 563 (1932); Wear v. Commissioner of Internal Revenue, 65 F. (2d) 665 (C. C. A. 3d, 1933); Camden Safe Deposit and Trust Company, 30 B. T. A. 287 (1934).

that some "benefits" might have been shifted, it denied that they "passed" under the exercise of donee's power.[15]

Though the court was justified in interpreting the power of appointment provision in the Federal Estate Tax statute as if the common law rules of vesting of future estates should govern, it is clear that it could have allowed the tax in this case without any strain of language.[16] In fact, allowing the tax would have been more consistent with the court's utterances upon similar problems involving the question whether a taxable transfer occurs where there has been a non-exercise, rather than an exercise of power. Thus when a settlor releases his entire interest in property by an inter vivos transfer, but retains the bare power to change the beneficiary, a taxable transfer occurs at the settlor's death, whether he exercises his power or not, and the property is included in his gross estate subject to the federal estate tax.[17] The same result has been reached in insurance cases where the insured retains the power to change his beneficiary but never exercises it.[18] These holdings are based upon the theory that the destruction of the power of control at death bestows an "economic benefit" upon the beneficiary which he did not have before.[19] This "economic benefit" theory is equally applicable to the instant case,[20] for the relationship of donee and donor's remaindermen logically cannot be distinguished from that of settlor, or in-

15. See Helvering v. Grinnell, 294 U. S. 153, 156, 157 (1935).

16. An early Treasury Regulation interpreting the instant provision in the Federal Estate Tax Act required that a tax be imposed on donee's estate irrespective of whether or not donee exercised his power of appointment. U. S. Treas. Reg. 68, Art. 24. This was subsequently changed. U. S. Treas. Reg. 70 (1929 ed.), Art. 24.

17. Reinecke v. Northern Trust Company, 278 U. S. 339 (1929); Helvering v. City Bank and Farmers' Trust Company, 74 F. (2d) 242 (C. C. A. 2d, 1934), cert. granted 55 Sup. Ct. 655 (1935). See ROBINSON, SAVING TAXES IN DRAFTING WILLS AND TRUSTS (2d ed. 1933) 204 et seq.

18. Chase National Bank v. United States, 278 U. S. 327, 63 A. L. R. 388 (1929). An additional element of control obtains in the insurance cases: insured may fail to pay his premiums and thus defeat his beneficiary. This factor does not appear to have been considered. A situation almost identical with the settlor cases would be a fully paid-up insurance policy, or an irrevocable trust set up to pay the premiums, with a power of control over the beneficiary reserved. See Comment (1935) 44 YALE L. J. 1409, 1415 et seq.; see also Oppenheimer, *Proceeds of Life Insurance Policies Under the Federal Estate Tax* (1930) 43 HARV. L. REV. 724.

19. See Burnet v. Wells, 289 U. S. 670, 678 (1933); Crooks v. Loose, 36 F. (2d) 571, 573 (C. C. A. 8th, 1929); (1935) 44 YALE L. J. 1245, 1247. This "economic benefit" theory has been used in other instances, even where there was no active power of control, to permit a succession tax upon vested interests which were subject to investment. Tyler v. United States 281 U. S. 497 (1930); Phillips v. Dime Trust and Safe Deposit Co., 284 U. S. 160 (1933); Moffit v. Kelly, 218 U. S. 400 (1910).

An analysis of the "economic benefits" which accrue to donor's remainderman yields the following: Donor's remainderman has a "right" to the remainder subject to a "liability" to divestment, because of donee's power of appointment or control. It is not until donee's death that this "liability" may be changed to an "immunity" to divestment, which is just as much a legal incident of ownership as is the "right." This change occurs whether donee exercises his power affirmatively in favor of donor's remainderman, or does not exercise it at all. For an analysis of the general problem, see Simes, *The Devolution of Title to Appointed Property* (1928) 22 ILL. L. REV. 480.

20. See Lee v. Commissioner of Internal Revenue, 57 F. (2d) 399, 402 (App. D. C. 1932); Wear v. Commissioner of Internal Revenue, 65 F. (2d) 665, 667 (C. C. A. 3d, 1933). These two cases have been overruled by the principal case.

sured, and beneficiary. In both cases, assuming the common law rule, a transfer of a vested interest, subject to divestment was made, and a bare power to change the beneficiary reserved. The fact that in the principal case the power was given to a donee, while in the others it was reserved by the settlor or insured is irrelevant.[21] Under the "economic benefit" theory, therefore, the remainder subject to donee's power of appointment might have been included in donee's taxable gross estate whether she specifically appointed donor's remaindermen or merely refrained from divesting them.[22]

It may be conceded that the language of the Federal Estate Tax Act, if strictly construed, would not justify a tax upon donee's estate in the absence of an affirmative exercise by donee of her power of appointment.[23] But the court might well have ruled oppositely in the instant case, since the donee affirmatively exercised her power in favor of donor's remainderman and complied with the language of the statute.

NEGOTIABILITY OF BONDS OF A MASSACHUSETTS TRUST

EVER since the Negotiable Instruments Law made form rather than function the test of negotiability, the application of that Act to long-term commercial paper has been a source of discontent. It is pointed out that bonds, debentures, and like instruments differ from bills and notes in a great many respects, and that the technical requirements of the statute have seriously limited the possibilities of inventing new types of negotiable instruments to meet the requirements of a rapidly changing financial world.[1] For instance, despite commercial usage, interim certificates were held to be non-negotiable because not payable in money.[2] In other cases mortgage provisions and certain kinds of references to the mortgage indenture have been held to make the promise in a bond conditional, thereby destroying its negotiability.[3] There have been similar holdings with respect to equipment trust certificates[4] and

21. See Saltonstall v. Saltonstall, 276 U. S. 260, 271 (1928).

The analogy of the settlor and insurance cases might be held inapplicable to the instant case upon the ground that the former two lines of cases had nothing to do with interpretation, but merely with the constitutionality of the federal estate tax provisions which provide for a tax in those specific instances. The same "economic benefit" rationale which was used in upholding constitutionality might equally as well have been used in the interpretation of the power of appointment provision of the Federal Estate Tax Act.

22. By the authority of the settlor and insurance cases, the "immunity" from divestment is transferred under the power, whether the power is exercised or not. The passage of this "immunity" is a sufficient basis to impose a tax upon the entire remainder. See Tyler v. United States, 281 U. S. 497, 502, 503 (1930); (1935) 44 YALE L. J. 1245, 1247, n. 19.

23. The Act provides that the power of appointment must be "exercised."

1. See Steffen and Russell, *The Negotiability of Corporate Bonds* (1932) 41 YALE L. J. 799, citing other articles; II MACHEN, MODERN LAW OF CORPORATIONS (1908) § 1740A. Cases on the application of the N. I. L. to bonds are collected in SMITH AND MOORE, CASES ON BILLS AND NOTES (3d ed. 1932) 1, n.

The Commercial Acts Section of the National Conference of Commissioners on Uniform State Laws has recommended amendments to the N. I. L. which would allow instruments to become negotiable through usage. HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS (1933) 150.

2. Manhattan Co. v. Morgan, 242 N. Y. 38, 150 N. E. 594 (1926).

3. King Cattle Co. v. Joseph, 158 Minn. 481, 199 N. W. 437 (1924); St. Louis-Carterville Coal Co. v. Southern Coal & Mining Co., 194 Mo. App. 598, 186 S. W. 1152 (1916).

4. Fidelity and Deposit Company v. Andrews, 244 Mich. 159, 221 N. W. 114 (1928).

municipal assessment bonds.[5] The question whether technical objections prevent the negotiability of the instruments of unincorporated associations is unsettled.[6] While New York has decided that the bonds of a joint stock company are negotiable,[7] this question with respect to the bonds of a Massachusetts trust was decided for the first time in a recent case. Replevin was brought to recover stolen debentures issued by the International Hydroelectric System, a voluntary association organized under the laws of Massachusetts. The instruments bore the statement that neither trustees nor shareholders assumed any personal liability. The court held for the plaintiff on the ground that since a Massachusetts voluntary association is not a legal person, the promise to pay was the promise of the trustees, and since the latter had agreed only to pay out of the assets held in trust, there was no unconditional promise within the meaning of Section 1 of the Negotiable Instruments Law.[8]

While the rationale of the instant case is justified by the rules of the common law and law merchant,[9] there is reason to believe that Section 191 of the Negotiable Instruments Law, defining "person" as including "a body of persons whether incorporated or not", was intended to endow business trusts with legal personality for the purpose of issuing negotiable instruments, and thus to change the former common law status of business trusts in this respect.[10] This view is supported by the interpretation given by the courts to Section 20, which provides: "Where the instrument contains or the person adds to his signature words indicating that he signs for or on behalf of a principal or in a representative capacity, he is not liable on the instrument if he was duly authorized." A number of cases have held that this section applies to relieve from personal liability a party who has signed a promissory note as trustee without inserting in the note any provision for limited liability.[11] The only basis upon which these decisions could have been reached is that the trustee was a representative signing on behalf of a disclosed principal, so that the trust estate and not the trustee was the promisor. While the liability of a trustee when limited to the extent of a particular fund would not be sufficient to satisfy the statutory requirement of unconditional liability of the promisor,[12] nevertheless, when the fund itself becomes the promisor, the requirement is met, the fund being unlim-

5. Manker v. American Savings Bank & Trust Co., 131 Wash. 430, 230 Pac. 406 (1924).

6. See Steffen, *A Proposed Uniform Act Making Investment Instruments Negotiable* (1934) 34 Col. L. Rev. 632; Handbook of the National Conference of Commissioners on Uniform State Laws and Proceedings (1933) 155. The Committee on Amendments to the Uniform Negotiable Instruments Act proposes to end the uncertainty by special recognition in the Act that unincorporated associations may issue negotiable instruments.

7. Hibbs v. Brown, 190 N. Y. 167, 82 N. E. 1108 (1907).

8. Lorimer v. McGreevy, 84 S. W. (2d) 667 (Kansas City Ct. of App., 1935), cert. denied, Mo. Sup. Ct. July 30, 1935, *sub. nom.* State ex rel. McGreevy v. Shain, J.

9. Taylor v. Davis, 110 U. S. 330 (1884); Larson v. Sylvester, 282 Mass. 352, 185 N. E. 44 (1933); Sears, Trust Estates as Business Companies (2d ed. 1921) §§ 32-34; Wrightington, Unincorporated Associations and Business Trusts (2d. ed. 1923) 224.

10. See Brannan, Negotiable Instruments Law (5th ed. 1932) 272; Note (1930) 5 Tulane L. Rev. 135.

11. Hawthorne v. Austin Organ Co., 71 F. (2d) 945 (C. C. A. 4th, 1934); Charles Nelson Co. v. Morton, 106 Cal. App. 144, 288 Pac. 845 (1930); Baker v. James, 280 Mass. 43, 181 N. E. 861 (1932); Megowan v. Peterson, 173 N. Y. 1, 65 N. E. 738 (1902); Restatement, Trusts (Tent. Draft, 1933) § 255, Comment (e). But cf. Vorachek v. Anderson, 54 N. D. 891, 211 N. W. 984 (1927) (N. I. L. not mentioned).

12. Daniel, Negotiable Instruments (6th ed. 1913) § 271; Tiedeman, Commercial Paper (1889) § 145.

itedly liable as an entity in the same manner that funds of a corporation may be liable for purposes of the Negotiable Instruments Law.[13]

There is nothing really novel in this conclusion, for the common law concept that a trust is not a legal person has already been abandoned for a number of other purposes. Statutes now permit voluntary associations and trusts to sue and be sued in their own names.[14] They are entities for the purposes of taxation[15] and bankruptcy.[16] They are included within the definition of a corporation in many states, and are regulated like corporations.[17] The United States Supreme Court has ruled that a Massachusetts voluntary association is a unit sufficiently distinct from its trustees so that it cannot claim the benefits assured to the latter by the privileges and immunities clause of Article IV, Section 2, of the Constitution, and thus may be excluded from a state as a foreign corporation.[18] From any other than the legal point of view a business trust is unquestionably an entity, quite as much so as a corporation.[19] Voluntary associations and trust estates function as business units, and there seems to be no good reason why their obligations, which perform all the functions of negotiable instruments, and which business men have treated as negotiable, should not be so regarded by the courts. Although custom does not prevail over legislation, a construction of the Negotiable Instruments Law which is incompatible with business usage is undesirable, and should not be followed in preference to an alternative view which is compatible with established legal principles.

ESTOPPEL OF TAXPAYER TO SET UP STATUTE OF LIMITATIONS WHERE GOVERNMENT IS LED TO DEFER TAX ASSESSMENT BY TAXPAYER'S MISREPRESENTATION OF LAW

EXECUTRIX desired to pay herself commission for services to the estate and to have the commission deducted in the computation of estate taxes. The amount of cash in the estate being insufficient, executrix lent it funds, taking back a note therefor, and thereafter paid herself the commission out of the funds lent. Although not including the commission in her income tax return of that year, she mentioned the transaction in a footnote, claiming that in accordance with the ruling by the Solicitor of Internal Revenue in an analogous case,[1] the commission was not taxable until it had been approved by the probate court. The district revenue agent at first rejected her claim, but after a conference, agreed to the executrix's interpretation, and accepted her return, anticipating the taxation of the commission when the court had approved it. Five years later the probate court approved the commission, and the revenue depart-

13. See BOGERT, TRUSTS AND TRUSTEES (1935) § 775; WARREN, CORPORATE ADVANTAGES WITHOUT INCORPORATION (1929) 864. Although the court in the instant case stated that it was greatly influenced by Professor Warren's attack upon the decision in Hibbs v. Brown, 190 N. Y. 167, 82 N. E. 1108 (1907), which held the bonds of a joint-stock company to be negotiable, (WARREN, op. cit. *supra* 477-500) it apparently failed to notice that the closing paragraph of this treatise supports the opposing view.

14. MASS. GEN. LAWS (1932) c. 182, § 6; cf. United Mine Workers v. Coronado Coal Co., 259 U. S. 344 (1922).

15. Hecht v. Malley, 265 U. S. 144 (1924).

16. Gallagher v. Hannigan, 5 F. (2d) 171 (C. C. A. 1st, 1925).

17. Reilly v. Clyne, 27 Ariz. 432, 234 Pac. 35, 40 A. L. R. 1005 (1925).

18. Hemphill v. Orloff, 277 U. S. 537 (1928).

19. See Sturges, *Unincorporated Associations as Parties to Actions* (1924) 33 YALE L. J. 383; Dodd, *Dogma and Practice in the Law of Associations* (1929) 42 HARV. L. REV. 977.

1. S. M. 1929, IV-1 Cum. Bull. 125.

ment then endeavored to tax it. Executrix, reversing her former position, now claimed that the commission was properly taxable in the earlier year, and that inasmuch as the Statute of Limitations had run as to tax claims for that year, the tax was uncollectible. The Board of Tax Appeals acquiesced in this defense, holding that inasmuch as the taxpayer's misrepresentation was one of law rather than of fact, the government could not invoke an estoppel against the taxpayer's denial of present taxability.[2]

The purpose of the Federal Statute of Limitations[3] as to tax claims is to prevent the taxpayer from being subjected to belated assessments which, being unexpected, may prove unduly burdensome. But since to preclude the government from collecting any income tax because of the running of the Statute of Limitations is to discriminate against those taxpayers who are taxed, it would seem desirable that the statute be allowed as a defense only in those instances where its purpose would be directly subserved. Thus, where the negligence of the tax unit is the sole reason for income not being taxed in a year now beyond the period of statutory limitation, it seems clear that such income should go untaxed in order to protect the taxpayer against unforeseeable liability not due to his own negligence or fraud.[4] This is true even where the taxpayer innocently makes an improper return, if at the same time he includes in his return sufficient facts to put the tax authorities on reasonable notice of the error, and those authorities negligently fail to correct the return before the statute has run.[5]

But where the taxpayer, although acting innocently, omits to include or misrepresents a fact which would alter his liability, and the tax authorities are not put on notice of the fact by the return, it would seem that, since the subsequent burdens placed on the taxpayer are virtually self-imposed, the taxpayer ought to be prevented from benefiting by the statute even though the factors of unexpectedness and consequent undue hardship of the tax assessment are present. In such cases it has been held that income may be taxed in the improper year, on the ground of equitable estoppel against the taxpayer.[6] And certainly where the taxpayer purposely makes an incorrect return with the intent of escaping that liability, it is obvious that the statute should not run against the government, since the purpose of the statute is solely to protect innocent taxpayers against unexpected tax assessments. In fact, the statute specifically exempts this last situation from its application.[7]

Finally, where, as in the principal case, the taxpayer represents as a matter of law that a portion of his income is taxable in a later year, and the government acquiesces in that claim, it would seem that the purpose of the statute is lost sight of, if, after the running of the period of limitations, the taxpayer is allowed to show

2. Richard M. Cadwalader, Jr., 32 B. T. A., Aug. 8, 1935.

3. 48 STAT. 745, 26 U. S. C. A. § 275 (1934).

4. Essex Coal Co. v. Commissioner, 39 F. (2d) 892 (C. C. A. 6th, 1930); United States v. S. F. Scott and Sons, Inc., 69 F. (2d) 728 (C. C. A. 1st, 1934).

5. Cf. Hamilton Web. Co. v. Page, 8 F. Supp. 626, 633 (D. R. I., 1934); see A. M. Johnson, 32 B. T. A. Feb. 26, 1935. The taxpayer usually is enabled to take advantage of the statute when the commissioner was warned of the error before the statute had tolled. See Helvering v. Brooklyn City Rr. Co., 72 F. (2d) 274, 276 (C. C. A. 2d, 1934); Union Pacific Rr. Co., 32 B. T. A., April 16, 1935, at 10.

6. Commissioner v. Liberty Bank & Trust Co., 59 F. (2d) 320 (C. C. A. 6th, 1932); Stern Bros. v. United States, 8 F. Supp. 705 (Ct. Cl., 1934); 2 POMEROY, EQUITY JURISPRUDENCE (4th ed. 1918) § 805; see Maguire and Zimet, *Hobson's Choice and Similar Practices in Federal Taxation* (1935) 48 HARV. L. REV. 1281, 1295.

7. 48 STAT. 745, 26 U. S. C. A. § 276(a) (1934); see Bert M. Wuliger, 16 B. T. A. 1220, 1225 (1929).

that the income was taxable in an earlier year and that assessment on it is now barred. For in such a case, if the taxpayer is acting in good faith, he intends to pay the tax in a subsequent year. Consequently he can make appropriate provision for its payment at that time, and the evils which may be attendant upon an unexpected and belated assessment, and which the statute is intended to prevent, cannot arise. If, on the other hand, the taxpayer has no intention of paying the tax, desiring merely to delay its assessment until it should be barred by the Statute of Limitations, he would seem to fall directly within that exception to the statute which denies the statute's protection to taxpayers fraudulently or intentionally endeavoring to evade income taxation.[7]

This result is the rule where the taxpayer and the commissioner agree upon a definite way of handling a situation, and it subsequently transpires that their interpretation was erroneous.[8] The taxpayer is held to his agreement and kept from showing the incorrectness of the mutual interpretation when the government taxes in accordance with that interpretation. Such an agreement need not be formal, but is usually implied in fact.[9] In the instant case, such an informal agreement appears to have been made, for, previous to the final acceptance of the tax return by the tax unit, the parties had discussed methods of taxing the executrix's commission, and it was finally decided that the commission should not be taxed until approved by the court.

But even if it be held that the elements of an agreement are lacking, still the taxpayer should be held liable for the taxes. Estoppel is denied for a misrepresentation of law[10] only because, all men being presumed to know the law, it is supposedly *prima facie* negligence to be misled by such a misrepresentation. But the present uncertainty in the tax law makes so theoretical an assumption utterly inappropriate for the practical problem of collecting revenue.[11] If the taxpayer gained, as he had

8. Backus et al. v. United States, 59 F. (2d) 242, 257 (Ct. Cl., 1932); see Ralston Purina Co. v. United States, 58 F. (2d) 1065, 1068 (Ct. Cl., 1932); Reynolds v. Gnichtel, 1 F. Supp. 606, 608 (D. N. J., 1932); Maguire and Zimet, *supra* note 6, at 1326. But generally the courts ignore the contractual aspect, reaching the same conclusion by various equitable approaches such as election, acceptance of benefits under previous error, or waiver of an inconsistent right. Cf. R. H. Stearns Co. v. United States, 291 U. S. 54 (1934); Hartwell Mills v. Rose, 61 F. (2d) 441, 444 (C. C. A. 5th, 1932); Moran v. Commissioner, 67 F. (2d) 601 (C. C. A. 1st, 1933); Wheelock et ux. v. Commissioner, 77 F. (2d) 474 (C. C. A. 5th, 1935); Naumkeag Steam Cotton Co. v. United States, 2 F. Supp. 126 (Ct. Cl., 1933); Mahoning Investment Co. v. United States, 3 F. Supp. 622 (Ct. Cl., 1933); Raleigh v. United States, 5 F. Supp. 622 (Ct. Cl., 1934); Stevens Mfg. Co. v. United States, 8 F. Supp. 720 (Ct. Cl., 1934); Giant Furniture Co. v. United States, 9 F. Supp. 585 (Ct. Cl., 1935); Louis Werner Saw Mill Co., 26 B. T. A. 141 (1932); J. O. W. Gravely, 29 B. T. A. 29 (1933), Firemen's Ins. Co., 30 B. T. A. 1004 (1934).

9. Ralston Purina Co. v. United States, 58 F. (2d) 1065, 1068 (Ct. Cl., 1932).

10. In many cases where estoppel is denied on the grounds that the misrepresentation is one of law, a careful analysis would seem to indicate that while the taxpayer's original error was one of law, the actual misrepresentation was one of fact, being the filing of a return which failed to mention at all the item of income in dispute. See Salvage v. Commissioner, 76 F. (2d) 112 (C. C. A. 2d, 1935), *cert. granted,* U. S. Sup. Ct., Oct. 14, 1935; Jamieson v. United States, 10 F. Supp. 321 (D. Mass., 1935); Union Pacific Rr. Co., 32 B. T. A., April 16, 1935. Estoppel has been allowed in similar cases. See Crane v. Commissioner, 68 F. (2d) 640 (C. C. A. 1st, 1934); Bothwell v. Commissioner, 77 F. (2d) 35 (C. C. A. 10th, 1935); Adler v. Commissioner, 77 F. (2d) 733 (C. C. A. 5th, 1935).

11. See Tide Water Oil Co., 29 B. T. A. 1208, 1218 (1934). Where the conclusion reached by denying estoppel against the taxpayer seems justifiable, it is usually because of the presence of obvious negligence on the part of the commissioner. See The Sugar Creek

expected, a deferral of his tax to a subsequent year, whether it was by a misrepresentation of fact or law, the injuries which the statute is intended to avert cannot fall on him, and he should not be granted tax exemption.[12]

RENT PAID BY LESSEE TO LESSOR'S STOCKHOLDERS AS INCOME TAXABLE TO LESSOR

IN 1881 the lessor corporation leased all its property to the lessee corporation for ninety-nine years, the lessee agreeing to maintain the property in good repair and to pay all taxes levied on the property in addition to an annual sum to the lessor to enable it to meet its corporate expenses. The lessee further agreed to pay a fixed rental directly to the lessor's bondholders and stockholders and, in pursuance of this agreement, executed its separate contract with each stockholder and bondholder upon his stock or bond certificate. The Commissioner of Internal Revenue attempted to include the payments to the bondholders and stockholders in the lessor's income[1] on the ground that the payments to the bondholders discharged a debt of the lessor to its creditors and that the payments to the stockholders should be treated as a distribution by the lessor of dividends. The Federal District Court for the District of Connecticut sustained the Commissioner's position with respect to the payments to bondholders. But it denied his contention that the payments to the lessor's stockholders were dividends, on the ground that the payments had never been due the lessor, but were a debt due by the lessee to the lessor's stockholders as donee-beneficiaries under the contract of lease.[2] In reaching this result, the court in effect overruled the previous federal rule.[3]

Coal and Mining Co., 31 B. T. A., Oct. 16, 1934; Hamilton Web Co. v. Page, 8 F. Supp. 626 (D. R. I., 1934); Union Pacific Rr. Co., 32 B. T. A. April 16, 1935.

12. Similar reasoning would seem to refute the validity of the present denial of estoppel for false expressions of opinion by the taxpayer. Summerfield Co., 29 B. T. A. 77 (1933); May Rogers, 31 B. T. A., Jan. 9, 1935; Northport Shores, Inc., 31 B. T. A. Jan. 15, 1935. Admittedly the commissioner must be held to a high standard of care in accepting opinions, but there are certain situations in which he should be held justified in relying on them.

1. 48 STAT. 686 (1934), 26 U. S. C. A. § 22 (1935); Eisner v. Macomber, 252 U. S. 189, 207 (1920) (income defined); see (1933) 28 ILL. L. REV. 572.

2. United States v. Northwestern Telegraph Co., 10 F. Supp. 703 (D. Conn. 1935). The government will appeal. 353 CCH Federal Tax Service p. 9061.

3. Anderson v. Morris & Essex Rr. Co., 216 Fed. 83 (C. C. A. 2d, 1914) (CORPORATE TAX ACT of 1909, 36 STAT. 112); Blalock v. Georgia Ry. & Electric Co., 246 Fed. 387 (C. C. A. 5th, 1917) (same); West End St. Ry. Co. v. Malley, 246 Fed. 625 (C. C. A. 1st, 1917) (one judge dissenting), cert. denied, 246 U. S. 671 (1918); Rensselaer & Saratoga Rr. Co. v. Irwin, 249 Fed. 726 (C. C. A. 2d, 1918) (one judge dissenting), cert. denied, 246 U. S. 671 (1918); Northern Ry. Co. of New Jersey v. Lowe, 250 Fed. 856 (C. C. A. 2d, 1918); American Telegraph & Cable Co. v. United States, 61 Ct. Cl. 326 (1925), cert. denied, 271 U. S. 660 (1926); 351 CCH Federal Tax Service ¶ 85.02 (collection of Treasury and Board of Tax Appeals rulings). Cf. Old Colony Trust Co. v. Comm'r of Internal Revenue, 279 U. S. 716 (1929) (payment by employer of employee's income tax held additional taxable income to employee); United States v. Boston & Maine Rr. Co., 279 U. S. 732 (1929) (payment by lessee corporation of lessor corporation's income and property taxes held additional taxable income to lessor). *Contra:* Northwestern Telegraph Co. v. Tax Comm., 212 Wis. 219, 248 N. W. 164 (1933), noted in (1933) 28 ILL. L. REV. 572, and in (1933) 11 N. Y. U. L. Q. REV. 303. The instant case also overrules a long series of Treasury Regulations. U. S. Treas. Reg. 86, Art. 70 (1934). Earlier regulations to the same effect were expressly approved in United States v. Boston & Maine Rr. Co., *supra*. By the enactment of a statute which has received an executive interpre-

The reasoning of the court seems to accord with that of the numerous cases of assignment, generally from husband to wife, to avoid income taxation. The rationale of these cases is vague,[4] aside from there being a general minimum requirement that an assignment, in order to transfer the tax liability to the assignee, must be irrevocable. In addition, the courts attempt to distinguish between assignments of "property rights" and assignments of mere income, holding that the former operate to transfer tax liability to the assignee, but that the latter have no such effect. Although the obvious difficulty of defining "property rights" necessitates a treatment of each case on its particular facts, rents have been considered "property rights" within the meaning of the rule.[5] Consequently, if these assignment cases be assimilated to those involving third party beneficiaries,[6] the promisee in the instant case would seem to be exempt from taxation, for the beneficiary has a right to the payment of rent, the irrevocable nature of which is demonstrated by the fact that the lessor can neither require the lessee to pay the rent to itself nor otherwise impair its shareholders' rights, once they have become vested,[7] without their consent.[8]

However, these analogies, taken primarily from cases of assignment between husband and wife to escape income taxation, become less persuasive in a case involving a corporation and its stockholders, where their application would result in the privileges of the corporate form being enjoyed without payment of the taxes prescribed therefor.[9] It is obvious in the instant case that the stockholders' rights to the rentals derive from their status as members of the corporation, disappearing when, by a transfer of their stock, they leave the corporation, and that the rent is paid for the use of the property of the corporation.[10] Furthermore, not only is the

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tation, where the interpretation has been generally acquiesced in by the courts, the executive becomes the legislative interpretation. See McCaughn v. Hershey Chocolate Co., 283 U. S. 488, 492 (1931).

The older rule holding the lessor liable had already been emasculated by decisions which in effect denied the government any means of collecting the tax. See notes 14, 16, *infra*. The instant case denied the existence of even the theoretical tax liability of the lessor.

4. See Comment (1929) 38 YALE L. J. 1123; Harwood v. Eaton, 68 F. (2d) 12, 14 (C. C. A. 2d, 1933) (Hand, J., concurring).

5. See Hall v. Burnet, 54 F. (2d) 443, 444 (App. D. C. 1931); cf. United States v. Looney, 29 F. (2d) 884 (C. C. A. 5th, 1929) (royalties); Nelson v. Ferguson, 56 F. (2d) 121 (C. C. A. 3d, 1932) (same). *Contra:* Lucas v. Earl, 281 U. S. 111 (1930) (attorney's fees); Burnet v. Leininger, 285 U. S. 136 (1932) (partnership income); Van Meter v. Comm'r of Internal Revenue, 61 F. (2d) 817 (C. C. A. 8th, 1932) (insurance commissions on renewals).

6. The only difference analytically is that an assignment requires a pre-existing right due the assignor, whereas in the case of a third party beneficiary contract the right is created in the same instrument in which it is transferred. The only difference in resulting jural relations is that the promisee in the latter case has an equitable right of action against the promisor for specific performance of his promise to the beneficiary, while the assignor completely surrenders all his rights, remedial as well as primary.

7. The right of a donee-beneficiary, unlike that of a creditor-beneficiary, becomes indefeasible immediately upon the formation of the contract. RESTATEMENT, CONTRACTS (1932) § 136, com. (a).

8. Bowers v. Interborough Rapid Transit Co., 121 Misc. 250, 201 N. Y. Supp. 198 (Sup. Ct. 1923), aff'd without opinion, 208 App. Div. 768, 202 N. Y. Supp. 917 (1st Dep't 1924); RESTATEMENT, CONTRACTS (1932) § 142.

9. 48 STAT. 686 (1934), 26 U. S. C. A. § 13 (1935); P. L. No. 407, 74th Cong., 1st Sess. (1935) § 102.

10. See West End Street Ry. Co. v. Malley, 246 Fed. 625, 626 (C. C. A. 1st, 1917); Harwood v. Eaton, 68 F. (2d) 12, 14 (C. C. A. 2d, 1933) (Hand, J., concurring).

corporate form a vital factor in the arrangement, but, since the entire net capital of the lessor remains unimpaired in the hands of the lessee[11] and the lessor corporation has no expenses whatever, the rent paid its stockholders for the use of its capital is tantamount to surplus derived therefrom, all of which is distributable. Therefore, just as a corporation is deemed to be enjoying a very real taxable income in the case of rentals paid by the lessee directly to the lessor's bondholders in discharge of the lessor's debts,[12] so, also, payments made directly to stockholders should be treated as a distribution of dividends and consequently as income of the corporation for purposes of taxation.[13] Both cases are similarly unique and both should be accorded exceptional treatment without any confusion of the issue by analogies drawn from the ordinary principles of third party beneficiary or of assignment.

There are admittedly practical difficulties in the way of collecting the lessor's tax. It has been held that, even if the lessor is liable to pay the tax, the government cannot recover the corporate tax from the shareholders, whether they be considered simply shareholders or "transferees" under the Revenue Act.[14] Furthermore, no obligation to pay the income tax of a lessor rests on the lessee;[15] nor can the government, under the lien statute, impress a lien on the funds in the hands of the lessee and restrain payments to the shareholders.[16] The only remedy thus left the government is the ordinary procedure of distraint and sale against the corporation's

11. If the lessor had to take care of depreciation, so much of the rent as would ordinarily be required to meet such charges would appear to be a capital distribution to shareholders.

12. Corporations have been held to owe their stockholders an equitable duty to declare dividends under certain circumstances. Reynolds v. Diamond Mills Paper Co., 69 N. J. Eq. 299, 60 Atl. 941 (1905); Dodge v. Ford Motor Co., 204 Mich. 459, 170 N. W. 668 (1919). To the extent, therefore, that the stockholders surrender their contingent rights to future dividends if earned, they may be considered creditor-beneficiaries rather than donees. But it is quite true that they are not creditors in the sense that bondholders are. American-Steel Foundries v. Lazear, 204 Fed. 204 (C. C. A. 3d, 1913); Godley v. Crandall & Godley Co., 212 N. Y. 121, 105 N. E. 818 (1914).

13. Some courts in situations like this stress the necessity of disregarding the lessor's corporate entity entirely and simply regarding the payments to stockholders as payments to their corporation. See Harwood v. Eaton, 68 F. (2d) 12, 14 (C. C. A. 2d, 1933) (Hand, J., concurring); Finkelstein, *The Corporate Entity and the Income Tax* (1934) 44 YALE L. J. 436; Comment (1932) 80 U. OF PA. L. REV. 892; cf. Sherman, *Taxation of Corporations Used to Avoid Taxes Upon Stockholders* (1935) 13 TAX M. 19, 78.

The holding of the instant court presents a possible scheme for future circumvention of the corporate income tax. For example, a corporation might lease its property to a subsidiary organized for the purpose at a rental to be paid directly to the shareholders of the parent corporation and fixed at such a high rate as to preclude any profit to the lessee. Since the rent would be deductible from the lessee's income as a business expense, 48 STAT. 688 (1934), 26 U. S. C. A. § 23 (1935), neither corporation would pay a tax and the only taxable income would be the payments to the stockholders of the lessor assessed against them individually.

14. 48 STAT. 748 (1934), 26 U. S. C. A. § 311 (1935); Harwood v. Eaton, 68 F. (2d) 12 (C. C. A. 2d, 1933), cert. denied, 292 U. S. 636 (1934); Western Union Telegraph Co. v. Comm'r of Internal Revenue, 68 F. (2d) 16 (C. C. A. 2d, 1933), cert. denied, 292 U. S. 636 (1934).

15. Sharon Ry. Co. v. Erie Rr. Co., 268 Pa. 396, 112 Atl. 242 (1920); Brainard v. New York Central Rr. Co., 242 N. Y. 125, 151 N. E. 152 (1926).

16. 45 STAT. 875 (1928), 48 STAT. 757 (1934), 26 U. S. C. A. §§ 1560-1567 (1935); United States v. Western Union Telegraph Co., 50 F. (2d) 102 (C. C. A. 2d, 1931), cert. denied, 292 U. S. 636 (1934), noted in (1931) 41 YALE L. J. 130. The statute provides

assets,[17] but it can distrain only against the reversion, which in a ninety-nine year lease is of negligible value. The problems of liability and collection, however, should be kept distinct.[18] The solution lies, not in denying a liability which obviously should exist, but in strengthening the collection procedure, perhaps by giving a more liberal judicial construction to the lien statute.[19]

that "such lien shall not be valid as against any mortgagee, purchaser or judgment creditor until notice of such lien shall be filed . . ." The court reasoned that, since no such provision against double liability is afforded a mere contract debtor like the lessee, the statute does not apply to an ordinary debt. It also held that the statute does not authorize garnishment.

17. 43 STAT. 343 (1924), 26 U. S. C. A. §§ 1580-1581 (1935). Theoretically the government might levy on the rents received by the stockholders, treating them as assets of the corporation, but such an attempt would have a doubtful fate. See Harwood v. Eaton, 68 F. (2d) 12, 15 (C. C. A. 2d, 1933) (Hand, J., concurring). Cf. Sherman, *supra* note 13, at 84.

Denial of the lessor's liability, which is unenforceable in any case, does result in the shareholders' paying normal individual income taxes on the rentals received by them, which would not be collectible if the payments were considered dividends, for dividends are deductible from an individual's normal tax and included only in his surtax. 48 STAT. 693 (1934), 26 U. S. C. A. § 25 (1935). However, this would obviously result in less revenue than the collection of the corporate tax plus the individual shareholders' surtaxes.

18. They have been confused by those holding the lessor not liable. See Northwestern Telegraph Co. v. Tax Comm., 212 Wis. 219, 224, 248 N. W. 164, 166 (1933); West End Street Ry. Co. v. Malley, 246 Fed. 625, 633 (C. C. A. 1st, 1917) (dissent). But in the lien and transferee cases the court was careful to base its decisions on procedural grounds. It assumed that the lessor would be liable for the tax. See notes 14, 16, *supra*.

19. See note 16, *supra*. The construction of the lien statute could be extended to include a contract debtor. See (1931) 41 YALE L. J. 130. If the courts refuse so to construe it, statutory action will be necessary.